90-1567

No.

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

ARDRA INSURANCE COMPANY, LTD., et al.,

Petitioners,

vs.

SALVATORE R. CURIALE, SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK, AS LIQUIDATOR OF NASSAU INSURANCE COMPANY, IN LIQUIDATION,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE NEW YORK STATE COURT OF APPEALS

PETITION FOR WRIT OF CERTIORARI

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April 9, 1991

QUESTIONS PRESENTED

1(a). Whether the New York State Court of Appeals is correct in holding that state insurance laws are generally exempt from United States statutes, or whether -- as this Court and the United States Courts of Appeals for the Fourth and Ninth Circuits have held -- the McCarran-Ferguson Act is the relevant federal statute and exempts only state regulation of the "business of insurance;" and

(b). Whether the New York Court of Appeals is correct in holding -- in direct conflict with the Fourth and Ninth Circuits -- that the liquidation of an insolvent insurance company falls within McCarran-Ferguson's exemption from federal law.

2. Whether the McCarran-Ferguson Act grants to the several states the power, where insurance is concerned, to

override the provisions of a United States treaty concerning international arbitration and the amendments to the federal Arbitration Act that implemented the treaty.

3. Whether the New York State Court of Appeals' judicially created law, denying arbitration in the liquidation of an insolvent insurance company, impermissibly erodes the strong federal policy -- here manifested in a treaty and in a statute -- favoring arbitration, and particularly favoring arbitration of disputes arising out of international commercial contracts.

LIST OF PARTIES AND RULE 29.1 LIST

Ardra Insurance Company, Ltd., has no subsidiaries and is wholly owned by the Corporate Holding Corporation, formerly Tiber Holding Corporation. Petitioners Richard A. DiLoreto and Jeanne S. DiLoreto were parties below.

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Ardra Insurance Company, Ltd., petitions for a writ of certiorari to review the judgment of the New York State Court of Appeals in this case.

OPINIONS BELOW

The opinion of the New York State Court of Appeals is not reported. It is reprinted in the Appendix at A:1-21.[1]

The opinion of the Supreme Court of the State of New York, Appellate Division-First Department, is reported at 156 A.D.2d 70, 553 N.Y.S.2d 695 (1st Dep't 1990). It is reprinted at A:22-35.

The orders of the Supreme Court of the State of New York, New York County, are not reported. The orders are reprinted at A:36-38 and A:39-56, respectively.

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[1] References to A:___ are to the appendix annexed to this petition; references to CA:___ are to the Petitioners' Appendix in the New York State Court of Appeals.

The opinion of the Court of Appeals for the Second Circuit is reported at 842 F.2d 31 (2d Cir. 1988). It is reprinted at A:57-84.

The opinion of the United States District Court for the Southern District of New York is reported at 657 F. Supp. 1223 (S.D.N.Y. 1987). It is reprinted at A:85-135.

JURISDICTION

The judgment of the New York State Court of Appeals was entered on December 20, 1990. On March 12, 1991, Justice Marshall extended the time for filing a petition for a writ of certiorari to and including April 9, 1991. The jurisdiction of this Court is invoked under 28 U.S.C. 1257(a).

CONSTITUTIONAL PROVISIONS, TREATY, AND FEDERAL STATUTES INVOLVED

The constitutional provisions involved in this petition are Article I, section 8, and Article VI, clause 2. These provisions are set forth at A:136-37.

The treaty involved in this petition is the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 21 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.S. 38, as implemented at 9 U.S.C. 201-208. The text of the treaty is set forth at A:138-53.

The United States statutes involved in this petition for certiorari are the Federal Arbitration Act, 9 U.S.C. 201-208, and the McCarran-Ferguson Act, 15 U.S.C. 1012(b). The texts of these statutes are set forth at A:154-59 and A:160, respectively.

STATEMENT

The Nassau Insurance Company ("Nassau") was incorporated in New York in 1964 and licensed as a stock casualty insurer the following year. CA:146. Ardra was incorporated in the Islands of Bermuda in 1976 for the purpose, among others, of providing a first layer of reinsurance for Nassau and spreading that risk among retrocessionaires. CA:148-49. When Nassau became insolvent, the Supreme Court, New York County, entered an order on June 22, 1984, liquidating Nassau and appointing former Superintendent of Insurance of the State of New York, James P. Corcoran (the "Liquidator"), as Nassau's liquidator pursuant to New York Insurance Law, article 74. A:60-61. The Liquidator took title to all of Nassau's property, contracts, and rights of

action, A:90-91, including three excess of loss reinsurance contracts with Ardra. A:88-89.

Ardra paid Nassau $3,804,070.35 in reinsurance proceeds prior to the liquidation. Ardra paid the Liquidator an additional $129,583.49 in reinsurance moneys after Nassau was liquidated. CA:151, 224. The reinsurance contracts allowed Ardra to associate, at its own expense, in the defense of claims against Nassau. CA:74, 83, 93. The Liquidator, however, repeatedly denied Ardra permission to associate in the defense of such claims. CA:158-66, 176-79. For that reason, Ardra's Board of Directors, meeting in Bermuda on February 19, 1985, voted to disclaim the contracts, and declined to make further payments. A:61, 91.

In April, 1985, the Liquidator commenced an action in Supreme Court, New

York County, against Ardra to recover reinsurance proceeds allegedly due under the reinsurance contracts. CA:218-38; A:131. The Liquidator alleged that he had performed all of N.ssau's obligations under the three reinsurance contracts. CA:225, 227, 229. Ardra moved to dismiss the action and compel arbitration under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "Convention"). A:6. While that motion was pending, Ardra removed the case to the United States District Court for the Southern District of New York, pursuant to 9 U.S.C. 205. A:61-62.

In the district court, Ardra again moved to compel arbitration. A:62. The Liquidator conceded that the reinsurance contracts contained written agreements that called for arbitration in Bermuda or the United States, that Bermuda and the United States are both signatories to the

Convention, that Ardra is a citizen of Bermuda, and that the "reinsurance agreements initially arose out of the commercial relationship between Ardra and Nassau." A:98. The district court, however, abstained and remanded the case to the state court. A:134-35. The United States Court of Appeals for the Second Circuit dismissed the appeal and denied mandamus. A:84. The Court of Appeals also held that "if the state court determines that the pertinent powers of the Superintendent are strictly derived from the rights of Nassau, and thus, are 'commercial,' the state court itself will be required, under the Supremacy Clause of the Constitution, to order arbitration pursuant to the Convention." A:75.

Following remand, Ardra moved again to compel arbitration under the Convention and the federal Arbitration Act.

The Liquidator renewed his cross-motion for summary judgment. A:25.

The trial court did not address Ardra's primary contention that the Convention and the implementing amendments to the federal Arbitration Act preempted any contrary state or federal law that would deny Ardra its right to arbitration. Instead, the court relied on the Liquidator's argument that the "McCarran-Ferguson act insulates him from the [f]ederal Arbitration Act." A:46. Ardra pointed out that the McCarran-Ferguson Act did not apply to this dispute for several reasons, including the fact that the Act preserves state regulation only of the "business of insurance." The Fourth Circuit had held that the liquidation of an insolvent insurance company did not constitute the "business of insurance" as that term is used in the Act. *Gordon v. Department of*

the Treasury, 668 F. Supp. 483, 490-91 (D. Md. 1987), *aff'd*, 846 F.2d 272 (4th Cir. 1988), *cert. denied*, 488 U.S. 954 (1988). The trial court, however, "decline[d] to adopt" the Fourth Circuit's holding in *Gordon* and denied the motion to compel arbitration. A:53. A month later, the Ninth Circuit reversed a district court order that disagreed with *Gordon* and also held that the Idaho laws relating to the liquidation of an insolvent insurer were "distinct from any 'business of insurance' situation envisioned by the McCarran-Ferguson Act." *Idaho ex rel. Soward v. United States*, 858 F.2d 445, 453 (9th Cir. 1988), *cert. denied*, 490 U.S. 1065 (1989).

Ardra appealed to the New York Supreme Court, Appellate Division-First Department, which unanimously affirmed the trial court's order, but on different grounds. The First Department did not

refer to either *Gordon* or *Soward*. Without any discussion, the court held that "[c]ertainly, the liquidation provisions of the [New York] Insurance Law were enacted 'for the purpose of regulating the business of insurance' (*see, S.E.C. v. National Securities, Inc. et al.*, 393 U.S. 453 [(1969)]; *Levy v. Lewis*, 635 F.2d 960 [(2d. Cir. 1980)]."[2] A:27. The First Department quoted portions of this Court's opinion in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985), but ruled against arbitration on the basis of an earlier decision of the New York State Court of Appeals, *Knickerbocker Agency, Inc. [Holz]*, 4 N.Y.2d 245, 173 N.Y.S.2d 602,

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[2] *National Securities* held that an Arizona insurance statute, pursuant to which the state's Insurance Director approved the merger of two insurance companies, was not "regulation . . . within the scope of the McCarran-Ferguson Act." 393 U.S. at 460. *Levy* is a decision on federal abstention.

149 N.E.2d 885 (1958).[3] The Court of Appeals held in *Knickerbocker* that the New York Supreme Court had exclusive jurisdiction of all actions involving a liquidated New York insurer, including those commenced by the liquidator, and that a New York trial court "may not be ousted of its jurisdiction in favor of an arbitrative tribunal" in a contract action commenced by the liquidator. 4 N.Y.2d at 252, 173 N.Y.S.2d at 608.

The First Department held, therefore, that under Article II(3) of the Convention and *Knickerbocker*, the arbitration agreements in the reinsurance contracts were "'null and void, inoperative or incapable of being performed.'" A:29.

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[3] *Knickerbocker* was decided before the Convention was drafted. It involved a purely intrastate dispute between the liquidator of an insolvent New York insurer and a broker residing in New York.

Ardra appealed to the New York State Court of Appeals which affirmed unanimously, but on yet other grounds. The Court of Appeals rejected one of the Liquidator's contentions and held that the "commercial" nature of the relationship between the parties had been determined at the time the reinsurance agreements were executed. Respondent's status as Liquidator did not transform his contract action into a "non-commercial" dispute. A:11-12. The court concluded, therefore, that the agreements "fall within the general scope of the Convention." A:12.

The court, nevertheless, held that certain exceptions contained in Articles II(1) and II(3) of the Convention applied. The court reasoned that, inasmuch as the McCarran-Ferguson Act provides that insurance is "generally a matter of State concern," there was no

reason why its decision in *Knickerbocker* should not be extended to bar arbitration under the Convention. A:14.

REASONS FOR GRANTING THE WRIT

This case merits plenary review for four reasons.

First, the New York State Court of Appeals' decision is in direct conflict with decisions of the United States Courts of Appeals for the Fourth and Ninth Circuits. In order to escape the Convention's requirement of arbitration, the New York court necessarily held that the liquidation of an insolvent insurer is state regulation of the "business of insurance" under the McCarran-Ferguson Act. The Fourth and Ninth Circuits have held squarely to the contrary. In so holding, those Circuits followed the clear definition of the "business of insurance" laid down by this Court. The

court below in this case ignored that definition.

Second, the New York court's decision nullifies provisions of the Convention, a United States commercial treaty with eighty-four foreign nations, and is contrary to this Court's holding in *Mitsubishi*. If the decision below stands, one result will be that the Convention is in force in many states but not in New York and in those states that choose to follow New York.

Third, the New York court's decision "seriously erode[s] federal policy" favoring arbitration. That, too, is contrary to *Mitsubishi*.

Fourth, this case is not only of great legal importance but of great practical significance as well. The State of New York is one of the nation's centers for both the insurance and reinsurance businesses. Arbitration

clauses are virtually universal in international reinsurance contracts. Hundreds of reinsurers are located in other countries that have adhered to the Convention and such reinsurers do business with United States insurers every day. As of year end 1989, in addition to Ardra, 1,313 international insurers were registered with the Bermuda Registrar of Companies. Bradford, *Bermuda: Still the Leader*, Business Insurance (Apr. 30, 1990) at 3. The overwhelming majority of these companies are reinsurers. In 1988, Bermuda-based insurers wrote gross premiums of more than $11.1 billion. *Id.* The decision below is certain to have a heavily adverse impact upon international commerce in reinsurance and is likely to lead to retaliatory action by other nations that have signed the Convention.

I

THE DECISION OF THE NEW YORK STATE COURT OF APPEALS CONFLICTS BOTH WITH DECISIONS OF THE FOURTH AND NINTH CIRCUITS AND WITH PRINCIPLES LAID DOWN BY THIS COURT

The question before the New York State Court of Appeals in this case was whether the Convention, a treaty of the United States implemented by the federal Arbitration Act, compelled arbitration according to the arbitration clauses in contracts between Nassau, an insolvent insurer, and Ardra, a Bermudan reinsurer. In refusing to enforce the arbitration clauses, the court held that the McCarran-Ferguson Act exempted from federal law state regulation of the liquidation of an insolvent insurer.

The Fourth and Ninth Circuits held squarely to the contrary in *Gordon*, 846 F.2d at 273-74, and *Soward*, 858 F.2d at 452. *Gordon* and *Soward*, and this Court's

decisions in *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982), and *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205 (1979), *reh'g denied*, 441 U.S. 917 (1979), hold that what McCarran-Ferguson preserves for state regulation is only the "business of insurance." Under all four decisions it is clear that state liquidation of an insolvent insurer is not regulation of the "business of insurance."

Ardra's reinsurance contracts with Nassau provided for arbitration of any dispute between the two companies. The State Superintendent of Insurance, as Nassau's liquidator, stands in the shoes of Nassau. When the Liquidator sued Ardra for reinsurance payments allegedly due, Ardra demanded arbitration and, since the contracts were international, invoked the Convention and the implementing amendments to the federal

Arbitration Act. 9 U.S.C. 201-208. The Convention commits the courts of acceding nations to recognize arbitration clauses contained in international commercial agreements and to enforce the resulting arbitral awards. Being a treaty of the United States, the Convention preempts any contrary state law because of the Constitution's Supremacy Clause. U.S. Const. art. VI.

The New York Court of Appeals, however, held to the contrary:

> In the United States statutes provide that insurance is generally a matter of State concern and that the laws of the individual states govern (McCarran-Ferguson Act, 15 USC §§ 1011, 1012[b], *supra*; *see also*, The Bankruptcy Act, 11 USC § 109[b][2] [which exempts insurance companies from its provisions]). Thus, in this case, the law to be applied in interpreting the exceptions is Article 74 of the New York Insurance Law.

A:14.

The federal Bankruptcy Act has no bearing on this case. McCarran-Ferguson merely declares Congress's policy that "continued regulation . . . by the several States of the business of insurance is in the public interest." 15 U.S.C. 1101. The only relevant and operative provision cited by the court was § 1012(b), which states in pertinent part:

> No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State *for the purpose of regulating the business of insurance* . . . unless such Act specifically relates to the business of insurance.

15 U.S.C. 1012(b) (emphasis added). The authority reserved to the states by § 1012(b) is only to regulate the "business of insurance."

The Fourth Circuit in *Gordon* held that state liquidation of an insolvent insurer is not regulation of the

"business of insurance." The court affirmed the district court which, applying the criteria laid down by this Court, concluded: "the liquidation of an insolvent insurance company and the priority of claims paid thereto does not constitute the 'business of insurance' as that term is used in the McCarran-Ferguson Act." 668 F. Supp. at 491.

The Ninth Circuit reached the same conclusion:

> In light of the insurers' insolvency and liquidation, there is no activity of an insurance company to be assessed. The companies have ceased to exist. . . . the nature of the insurance companies' "activities" is a moot question. Their activities have ceased just as they themselves have ceased to exist--leaving behind a finite pool of assets which the State of Idaho seeks to distribute according to its own plan. This is distinct from any "business of insurance" situation envisioned by the McCarran-Ferguson Act.

Soward, 858 F.2d at 453.

The Fourth and Ninth Circuits followed this Court's rulings in *Pireno* and *Royal Drug*. *Pireno* held that an insurance company's use of a peer review committee to set "reasonable" chiropractor's fees was not exempt from the antitrust laws under McCarran-Ferguson. The Court restated the three criteria which define whether a practice is part of the "business of insurance:"

> *first*, whether the practice has the effect of transferring or spreading a policyholder's risk; *second*, whether the practice is an integral part of the policy relationship between the insurer and the insured; and *third*, whether the practice is limited to entities within the insurance industry.

458 U.S. at 129 (emphasis the Court's).

These criteria make it clear that the Fourth and Ninth Circuits were correct and the New York Court of Appeals wrong.

(1) Liquidation procedures do not have the "effect of transferring or spreading a policyholder's risk." The question in liquidation is simply one of collecting from those who owe the insolvent company money and paying the claims of creditors. The policyholders stand in parity with other claimants. (2) Nor are the liquidation procedures an "integral part of the policy relationship between the insurer and the insured." This criterion relates to the "type of policy which could be issued, its reliability, interpretation, and enforcement." *Id.* at 128. Liquidation procedures have nothing to do with such subjects. (3) Liquidation procedures are certainly not "limited to entities within the insurance industry." A great number and variety of persons who supplied goods and services to the

insolvent company will have their claims determined in the liquidation.

If the claims adjustment process of an active insurance company was held not to be the "business of insurance" in *Pireno*, then most certainly the liquidation of a defunct insurer is not that business.

The New York State Court of Appeals did not even attempt to apply the *Pireno* criteria. It simply said that McCarran-Ferguson meant that the insurance laws of the individual states govern. This was the mistake identified in *Royal Drug*: "[t]he exemption is for the 'business of insurance,' not the 'business of insurers.'" 440 U.S. at 211. Indeed, the New York court widened the exemption even further, holding that it covered all state laws concerning insurance companies, even those companies no longer in business.

The court below created a McCarran-Ferguson Act exemption that sweeps more broadly than its destructive effect upon arbitration clauses. By reading the Act to exempt from federal law all state law in any way touching upon the subject of insurance, the court below nullified federal statutes giving the United States priority for its claims in liquidation proceedings and would, contrary to *Pireno*, entirely exempt anything insurance companies do from such federal laws as the Sherman Act.

The conflict between the state court here and the Fourth and Ninth Circuits, as well as with decisions of this Court, is important and should be resolved.

II

THE DECISION OF THE NEW YORK STATE COURT OF APPEALS NULLIFIES PROVISIONS OF A UNITED STATES TREATY

In *Mitsubishi*, 473 U.S. 614, this Court held that "concerns of international comity, respect for the capacities of foreign and transnational tribunals, and sensitivity to the need of the international commercial system for predictability in the resolution of disputes require that we enforce the parties' agreement [to arbitrate], even assuming that a contrary result would be forthcoming in a domestic context." *Id.* at 629.

Mitsubishi concerned the same Convention at issue in the present case, and the same factors that led the Court to enforce the arbitration agreement there are present here. Reinsurance contracts are usually international and

they almost universally contain arbitration clauses. If states can nullify the Convention with their own policies respecting arbitration, damage is done to international comity, disrespect is shown for foreign and transnational tribunals, and unpredictability is built into the international commercial system.

The Court refused in *Mitsubishi* to imply an exception to the Convention for Sherman Act cases even though every court of appeals that had ruled on the question -- the First, Second, Fifth, Seventh, Eighth, and Ninth Circuits -- had done so. The Court noted that it faced a "judicially implied exception:" "But we decline to subvert the spirit of the United States' accession to the Convention by recognizing subject-matter exceptions where Congress has not

expressly directed the courts to do so." *Id.* at 639 n.21.

In the present case, too, we face a judicially implied exception. But not one implied by federal courts of appeals for a policy as important as the Sherman Act; rather the exception here is one implied by New York's Court of Appeals for a policy as trivial as preventing the liquidator of insolvent insurance companies from litigating in any forum other than New York's trial courts. The policy giving rise to the implied exception to the Convention is not even consistently followed, for the Liquidator litigates in other forums whenever it is in his interest to do so.

In this point, we show that, however the "business of insurance" is defined, McCarran-Ferguson does not save New York's judicial policy against arbitra-

tion from the contrary commands of the Convention.

The court below recognized that under the Supremacy Clause, "[a]ny Federal or State law that 'prevents the Federal Government from "speaking with one voice" in international trade' must bow to [the] superior authority" of a United States treaty. A:7-8 (quoting *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 453-54 (1979)). The court held that the reinsurance contracts at issue in this case fell "within the general scope of the Convention." A:12. The court also said that if the Convention applied, it clearly preempted not only the McCarran-Ferguson Act, but any contrary provision

in the New York State Insurance Law as well.[4] A:8.

The New York Court of Appeals nevertheless said that the McCarran-Ferguson Act means that matters relating to insurance are governed by the states. Hence, the judicially implied policy of New York prevented the Liquidator from arbitrating.

The court reached consideration of the McCarran-Ferguson Act, however, only by relying on the Convention itself. The court said that the relevant Article II exceptions "require recognition of an arbitral agreement only when it 'concern[s] a subject matter capable of settlement by arbitration' and provide that the court of an acceding nation may

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[4] There is, however, no provision in Article 74 of the New York Insurance Law that bars arbitration when the liquidator of an insolvent New York insurer asserts a claim under a contract containing an arbitration clause. We are dealing here with a judicially implied New York State policy against such arbitration.

refuse to refer disputing parties to arbitration if the international agreement 'is null and void, inoperative or incapable of being performed.'" A:13. The court thus relied, respectively, on Article II(1) and (3). It was entitled to rely upon neither.

This Court's ruling in *Mitsubishi* that Sherman Act claims must be referred to an arbitration panel sitting in Tokyo, in accordance with the contract, means that very few, if any, subject matters are to be considered not "capable of settlement by arbitration." Certainly, in the light of *Mitsubishi* and *Scherk v. Alberto-Culver Co.*, 417 U.S. 506 (1974), *reh'g denied*, 419 U.S. 885 (1975), in which a claim arising under the Securities and Exchange Act of 1934 was held arbitrable pursuant to a provision in an international contract, the question of whether the Liquidator was required by

contract to allow Ardra to associate itself in the defense of claims made against Nassau is a subject entirely capable of settlement by arbitration.

As one authority on commercial arbitration has written,

> [i]t would appear that following the Mitsubishi decision, Article II(1) of the Convention, will be of little use to parties seeking the assistance of courts in the United States to stop the arbitration process at the stage of the enforcement of the arbitration agreement.

Domke on Commercial Arbitration § 44:04 (G. Wilner rev. ed. 1984, Supp. 1990).

Article II(1) is not a warrant for a state court to look to a policy against arbitration that the court itself created. In any event, the exception of Article II(1) applies to subject matters that do not lend themselves to arbitration, not to the forum in which a state court prefers to have disputes resolved.

The New York court converted an exception for subject matters to an exception that allows a state to override the parties' choice of forum. That is a distortion of the Convention.

It also seems highly probable that the Convention's drafters intended that only Congress could make domestic exceptions to arbitrability under the Convention. This Court in both *Scherk* and *Mitsubishi* pointed to the

> Convention delegates' frequent[ly voiced] concern that courts of signatory countries in which an agreement to arbitrate is sought to be enforced should not be permitted to decline enforcement of such agreements on the basis of parochial views of their desirability or in a manner that would diminish the mutually binding nature of the agreements.

Mitsubishi, 473 U.S. at 639 n.21; *Scherk*, 417 U.S. at 520 n.15. This Court, therefore, refused to recognize a

judicially implied exception not made by Congress:

> Congress may specify categories of claims it wishes to reserve for decision by our own courts without contravening this Nation's obligations under the Convention. But we decline to subvert the spirit of the United States' accession to the Convention by recognizing subject-matter exceptions where Congress has not expressly directed the courts to do so.

Mitsubishi, 473 U.S. at 639 n.21.

These statements by the Court are entirely consistent with a reading of the exceptions to mean, in the case of Article II(1), that only Congress, and not a state, may declare that a subject matter is not "capable of settlement by arbitration." That reading, which is the most plausible, and the most consistent with the Convention delegates' concerns and this Court's language, provides an additional reason why New York's judicially implied exception to the

Convention is an impermissible nullification of the Convention.

Nor is Article II(3) relevant to the issue of whether disputes arising under reinsurance contracts must be arbitrated. Article II(3) has been narrowly interpreted to apply only to "internationally recognized defenses such as duress, mistake, fraud, or waiver" or a violation of the fundamental policies of the forum nation. *Rhone Mediterranee Compagnia Francese v. Lauro*, 712 F.2d 50, 53 (3d Cir. 1983); *Ledee v. Ceramiche Ragno*, 684 F.2d 184, 187 (1st Cir. 1982); *I.T.A.D. Assocs. v. Podar Bros.*, 636 F.2d 75, 77 (4th Cir. 1981); *Oriental Commercial & Shipping Co. v. Rosseel, N.V.*, 609 F. Supp. 75, 78 (S.D.N.Y.

1985). None of these defenses has been raised here.[5]

The inapplicability of Article II's exceptions to an agreement to arbitrate the right of a reinsurer to associate in the defense of claims against the insurer is itself dispositive of this case. But that is not the only hurdle the court below failed to clear.

If the New York court's interpretation of the Convention's exceptions

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[5] The court below found that its interpretation of Article II(3) was "also supported by Article V of the Convention which specifies when arbitral awards may be denied recognition." A:17. In *dicta*, the court opined that, under Article V(2)(a), arbitration of the dispute would be "futile" because New York courts would refuse to enforce any award against the Liquidator. A:17. This conflicts with this Court's direction in *Mitsubishi* that national courts should not "speculate" on the enforceability of an award when asked to recognize an arbitral agreement. *Mitsubishi*, 473 U.S. at 637-38; *see Bergesen v. Joseph Muller Corp.*, 710 F.2d 928, 933 (2d Cir. 1983). Indeed, the New York Court of Appeals in an earlier decision held that the very purpose of the Convention was to minimize "significant judicial intervention until *after* an arbitral award is made." *Cooper v. Ateliers de la Motobecane*, 57 N.Y.2d 408, 416, 456 N.Y.S.2d 728, 732, 442 N.E.2d 1239 (1982) (emphasis the court's).

were proper, the court would still have had to use the McCarran-Ferguson Act to reach the New York policy of refusing to allow the Liquidator to arbitrate. Assuming, *arguendo*, that McCarran-Ferguson would have the effect the court gave it domestically, the Act does not shield an international contract from the force of the Convention and the Arbitration Act.

To begin with, the McCarran-Ferguson Act was intended to apply only to interstate commerce. It was enacted for the limited purpose of overruling this Court's decision in *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), *reh'g denied*, 323 U.S. 811 (1944), which had reversed the rule that the business of insurance was *not* interstate commerce within the meaning of the Commerce Clause. *See Paul v. Virginia*, 75 U.S. (8 Wall.) 168, 183

(1869). Congress sought in enacting McCarran-Ferguson merely to return matters to the *status quo ante*. H.R. Rep. No. 143, 79th Cong., 1st Sess., *reprinted in* 1945 U.S. Code Cong. & Admin. News 670, 671-2.

The Senate debates on McCarran-Ferguson make clear that it applies only to interstate commerce. Senator Ferguson himself stated:

> If there is on the books of the United States a legislative act *which relates to interstate commerce*, if the act does not specifically relate to insurance, it would not apply at the present time. Having passed the bill now before the Senate, *if Congress should tomorrow pass a law relating to interstate commerce, and should not specifically apply the law to the business of insurance, it would not be an implied repeal of this bill, and this bill would not be affected, because the Congress had not, under subdivision (b), said that the new law specifically applied to insurance*. I think that [my explanation] makes the bill very clear.

91 Cong. Rec. S340 (Jan. 25, 1945) at 481 (emphasis added). Senator Revercomb's comments are to the same effect. *Id.* at 485.

The federal Arbitration Act, 9 U.S.C. 202, also makes clear that purely interstate or intrastate disputes do not come within the confines of the Act: "An agreement or award arising out of [a legal commercial] relationship which is entirely between citizens of the United States shall be deemed not to fall under the Convention unless" there is some "reasonable relation with one or more foreign states." Thus, the states are permitted to regulate interstate commerce in insurance.

The Convention, however, deals entirely with arbitration in international commercial matters. The Senate's accession to the Convention and Congress's amendments to the Arbitration

Act are clearly exercises of Congress's exclusive power "To regulate Commerce with foreign Nations." U.S. Const. art. I, § 8, cl. 3. The McCarran-Ferguson Act, operating solely on interstate commerce, saves nothing from federal regulation of foreign commerce. To hold otherwise would be to say that McCarran-Ferguson, on the subject of insurance, granted to the states power to supersede treaties of the United States. That can never be imagined to have been the intention of Congress.

"Foreign commerce is pre-eminently a matter of national concern." *Japan Line*, 441 U.S. at 448. In that case, a California tax on Japanese instrumentalities of foreign commerce was struck down "because it prevent[ed] the Federal Government from 'speaking with one voice' in international trade." *Id.* at 453. The tax in *Japan Line* was invalidated by

the dormant congressional power over foreign commerce. In this case, New York has interfered with an actual exercise of the foreign commerce power. Although paying lip-service to the principle that no state court can prevent the United States from "speaking with one voice" in international trade, A:8, that is precisely what the Court of Appeals did.

In fact, the judicially created policy of New York, which the court held strong enough to avoid the Convention and the Arbitration Act, is often ignored. The basis of the policy is supposedly that the statute gives exclusive jurisdiction to claims *against* the insolvent insurer to the New York Supreme Court. The court has broadened the policy to apply to claims *by* the Liquidator. But, in fact, he participates in proceedings in courts in other states, when it suits his purpose. *Columbus-America Discovery*

Group, Inc. v. Unidentified, Wrecked, & Abandoned Sailing Vessel, 742 F. Supp. 1327, 1344 (E.D. Va. 1990); *Bohlinger v. Kagan*, 147 F. Supp. 910 (D.R.I. 1956); *Holz v. H.C. Baldwin Agency, Inc.*, 140 F. Supp. 860 (S.D. Ind. 1956). If the Liquidator may not arbitrate one issue with Ardra because of the exclusive jurisdiction of the New York Supreme Court, it is difficult to understand why he may litigate other issues in other courts. The New York Court of Appeals' "policy" seems no more than hostility to arbitration.

It cannot be said that arbitration is unsuited to the liquidation process. The rehabilitators and liquidators of insolvent insurance companies in other states have recently arbitrated disputes with the Bermudan reinsurers of insolvent American insurers. *See, e.g., Transit Casualty Co. v. Trenwick Reinsurance Co.*,

659 F. Supp. 1346 (S.D.N.Y. 1987), *aff'd*, 841 F.2d 1117 (2d Cir. 1988); *Mutual Fire, Marine & Inland Ins. Co. v. Norad Reinsurance Co.*, 868 F.2d 52 (3d Cir. 1989). A Bermudan reinsurer is thus apparently entitled to arbitrate a contract dispute with the liquidator of an insolvent insurer domiciled in Missouri or Pennsylvania, but not with an insurer domiciled and being liquidated in New York.

Federal and state courts, moreover, have directed that liquidators of insolvent insurers arbitrate their disputes with American reinsurers under the federal Arbitration Act. *Bennett v. Liberty Nat'l Fire Ins. Co.*, No. CV 90-17-H-CCL (D. Mont., Helena Div. Jan. 9, 1991); *Ainsworth v. Allstate Ins. Co.*, 634 F. Supp. 52, 57 (W.D. Mo. 1985); *Universal Marine Ins. Co. v. Beacon Ins. Co.*, 592 F. Supp. 948 (W.D.N.C. 1984);

Fabe v. Columbus Ins. Co., No. 89 AP-869 (10th App. Dist. Ohio June 26, 1990). Thus, some reinsurers domiciled in the United States have been accorded their contractual right to arbitration, while reinsurers domiciled in other nations that have adhered to the Convention have been denied the same right.

Selective application of the Convention, depending upon the policy of each state, breaks the international promises this nation made. The Fifth Circuit recognized what was at stake in a case arising under the same Convention. It remanded the case with directions to compel arbitration "in order to prevent the United States from violating its Treaty obligations with 65 [now 84] nations." *Sedco, Inc. v. Petroleos Mexicanos Mexican Nat'l Oil Co.*, 767 F.2d 1140, 1149 (5th Cir. 1985).

This is not the first time that a New York Superintendent of Insurance, acting as the liquidator of an insolvent insurer, has "collide[ed] with and subtract[ed] from" United States foreign policy. *United States v. Pink*, 315 U.S. 203, 231 (1942). In *Pink*, the Superintendent liquidated the United States branch of a Russian insurance company and sought to distribute the proceeds of the estate contrary to the terms of certain Executive Agreements recognizing the Soviet Government.

The United States brought suit against the liquidator and the New York State Court of Appeals affirmed a dismissal of that action. This Court reversed, stating:

> If state laws and policies did not yield before the exercise of the external powers of the United States, then our foreign policy might be thwarted. These are delicate matters. If state action could defeat or

> alter our foreign policy, serious consequences might ensue.

Id. at 232. This Court pointed out that no state "can rewrite our foreign policy to conform to its own domestic policies" and quoted an earlier decision in which the Court held:

> In respect of all international negotiations and compacts, and in respect of our foreign relations generally, state lines disappear. As to such purposes the state of New York does not exist.

Id. at 234 (quoting *United States v. Belmont*, 301 U.S. 324, 331 (1937)).

The Court of Appeals' judgment creates the basis for retaliatory actions by the legislatures or courts of other nations that have acceded to the Convention. It thus creates the "legal no-man's land" that Congress sought to eliminate when it implemented this treaty. *Scherk*, 417 U.S. at 516-17; *see Mitsubishi*, 473 U.S. at 631.

Review should be granted here so that the New York Court's attempt to set its policies above those of the Convention and the Congress may be set aside.

III

THE ORDER BELOW WOULD "SERIOUSLY ERODE FEDERAL POLICY" FAVORING ARBITRATION, PARTICULARLY WHERE THE ARBITRATION AGREEMENTS ARE CONTAINED IN INTERNATIONAL CONTRACTS

The decision of the New York State Court of Appeals manifests a strong hostility to arbitration that is squarely in conflict with federal policy, statutes, and this Court's decisions. In *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989), the Court stated that "suspicion of arbitration as a method of weakening the protections afforded in the substantive law . . . has fallen far out of step with our current strong endorsement of the

federal statutes favoring this method of resolving disputes." 490 U.S. at 481. Questions of arbitrability "should" be addressed with a "healthy regard for the federal policy favoring arbitration" and "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration." *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983).

The decision below rests upon explicit hostility to arbitration. The authority the court relied on was its own 1958 *Knickerbocker* decision which held that the New York Superintendent of Insurance, as liquidator of an insolvent insurer, was not bound by the arbitration clause in the contracts he assumed. The New York Insurance Code gave exclusive jurisdiction to the Supreme Court over claims *against* the insurance company in liquidation, but had no similar provision

as to claims *by* the liquidator. The New York Court of Appeals, over a strong dissent, nevertheless held that exclusive jurisdiction over the latter class of suits was to be implied and that the liquidator could not be compelled to arbitrate. In doing so, it repeatedly manifested hostility to arbitration.[6]

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[6] The court quoted with approval the statement of the Appellate Division in a different kind of case: "It was not intended *without express statutory authorization* that arbitrators, who are private individuals, who are subject to selection by the parties themselves * * * and who are charged with no public trust, should determine these matters." 4 N.Y.2d at 251 (emphasis and ellipsis by the *Knickerbocker* court). To make its hostility clear, the court guessed at the reason that the legislature had not authorized the liquidator to arbitrate by quoting from *Bernhardt v. Polygraphic Co. of Am. Inc.*, 350 U.S. 198, 203 (1956):

> "The change from a court of law to an arbitration panel may make a radical difference in ultimate result. * * * Arbitrators do not have the benefit of judicial instruction on the law; they need not give their reasons for their results; the record of their proceedings is not as complete as it is in a court trial; and judicial review of an award is more limited than judicial review of a trial * * *."

4 N.Y.2d at 253 (ellipses the court's). The *Bernhardt* rationale has long since been abandoned

(continued...)

The New York Court of Appeals in the present case not only relied upon *Knickerbocker*, but actually said that hostility to arbitration was a proper consideration in interpreting the Convention:

> [Exceptions to the Convention] are properly construed to effect New York's strong public policy concerns by maintaining Supreme Court's exclusive jurisdiction over liquidation proceedings. Arbitrators are private individuals, selected by the contracting parties to resolve matters important only to them. They have no public responsibility and they should not be in a position to decide matters affecting insureds and third party claimants after the contracting party has failed to do so.

A:17-18.[7]

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[6](...continued)
by this Court.

[7] The New York court's argument sounds very much like

> [t]he argument that . . . [choice of forum] clauses are improper because they tend to "oust" a court of

(continued...)

The court below actually expanded the holding of *Knickerbocker*, which stressed that "we are not here concerned with nonresidents." 4 N.Y.2d at 254 (emphasis the court's). The court here, however, extended *Knickerbocker's* hostility to domestic arbitration to international arbitration without recognizing that "domestic notions of arbitrability" do not extend to the international sphere. *Scherk*, 417 U.S.

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[7](...continued)
jurisdiction [and] is hardly more than a vestigial legal fiction. It appears to rest at core on historical judicial resistance to any attempt to reduce the power and business of a particular court and has little place in an era when all courts are overloaded and when businesses once essentially local now operate in world markets.

M/S Bremen v. Zapata Off-Shore Co., 407 U.S. 1, 12 (1972).

at 508, 519-20 (claim arising under the Securities Exchange Act of 1934).[8]

The failure to direct the parties to proceed to arbitration was clearly erroneous. Federal substantive law, applicable in state as well as federal courts, controls this case, not New York State policies derived from judicial exceptions to arbitration. *Moses H. Cone*, 460 U.S. at 24; *Southland Corp. v. Keating*, 465 U.S. 1, 12 (1984).

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[8] National courts, both before and after *Mitsubishi*, have consistently held that "domestic notions of arbitrability" do not apply to international commercial agreements that fall within the Convention. *Genesco, Inc. v. T. Kakiuchi & Co.*, 815 F.2d 840, 845-6 (2d Cir. 1987) (RICO claims); *In re Mor-Ben Ins. Mkts. Corp.*, 73 Bankr. 644, 647 (9th Cir. 1987); *In re Hart Ski Mfg. Co.*, 18 Bankr. 154, 158-59 (Bankr. D. Minn. 1982), *aff'd*, 711 F.2d 845 (8th Cir. 1983); *In re Fotochrome, Inc.*, 377 F. Supp. 26, 30-31 (E.D.N.Y. 1974), *aff'd sub nom. Fotochrome, Inc. v. Copal Co.*, 517 F.2d 512 (2d Cir. 1975) (bankruptcy-related claims); *Bird v. Shearson/American Express Inc.*, 871 F.2d 292 (2d Cir. 1989), *vacated and remanded*, 110 S. Ct. 225 (1989), *remanded with directions to send to arbitration*, 1991 WESTLAW 3220 (2d Cir. Jan. 17, 1991) (ERISA claims).

The strong federal policy favoring arbitration, as already noted, is even stronger in the context of international trade. "Such a contract involves considerations and policies significantly different from those found controlling" for a contract with no international aspects. *Scherk*, 417 U.S. at 515. *Mitsubishi* enumerated the special factors, *see supra* at p. 25, that require enforcement of an international arbitration agreement "even assuming that a contrary result would be forthcoming in a domestic context." 473 U.S. at 629. Moreover, "a problem that might be deemed *de minimus* in a domestic context [ ] assumes importance when sensitive matters of foreign relations and national sovereignty are concerned." *Japan Line*, 441 U.S. at 456.

It was Congress's intent that the federal Arbitration Act "move the parties

to an arbitrable dispute out of court and into arbitration as quickly and easily as possible." *Moses H. Cone*, 460 U.S. at 22.

Congressional intent has already been frustrated in this case. Petitioner Ardra demanded arbitration in May, 1985, and moved to compel arbitration in June, 1985, approximately three weeks before this Court decided *Mitsubishi*. Any further delay "would defeat the core purpose of a contract to arbitrate." *Southland*, 465 U.S. at 7-8.

The New York Court of Appeals order frustrates a strong federal policy favoring arbitration, an even stronger federal policy favoring international commercial arbitration, and Congress's exercise of its exclusive power to regulate foreign commerce. The judgment below merits review by this Court.

IV

THE ISSUES PRESENTED BY THIS CASE ARE IMPORTANT TO THE INSURANCE INDUSTRY AND OTHER REPRESENTATIVES OF THE AMERICAN BUSINESS COMMUNITY

This country has recently experienced an unprecedented number of insurance company insolvencies. *Failed Promises: Insurance Company Insolvencies*, Report by the Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce (Feb. 1990) ("Dingell Report") at 2. More than 150 United States property/casualty insurers have been liquidated since 1969, with half of these insolvencies occurring over the past five years. *Id.* There is little to suggest that this will soon change. In 1987, the National Association of Insurance Commissioners designated 21.4% of the property/casualty insurers it examined for "regulatory attention," up from 8.4% in 1978. Rappaport, *CRS Report*

for Congress: Insurance Company Solvency (Congressional Research Service Monograph, July 13, 1989) at CRS-8.

As a consequence, state insurance departments exercise control over literally dozens of insolvent insurers. In New York, for example, the Superintendent of Insurance is currently responsible for the liquidation, rehabilitation, or conservation of approximately sixty companies. *One Hundred Thirty-First Annual Report of the Superintendent of Insurance* (1989) at 204-5; Office of the State Comptroller, *New York State Insurance Department: The Liquidation Bureau: Insurance Company Estates Are At Risk Because of Inadequate Controls and Deficient Operating Procedures*, Report no. 90-S-76 (1990) at MS-1.

Many of the recent insolvencies in New York and other states "involve

complex multi-national companies, whose failures are felt around the world." Semaya, *Insurer Insolvency: Where We Are Today*, Law and Practice of Insurance Company Insolvency Revisited (ABA 1989) at 3-4. Reinsurers located outside the United States are directly affected by these failures because reinsurance is and always has been, in very substantial measure, an international business. 1 K. Gerathewohl, *Reinsurance Principles and Practice* 649 (1982); Dingell Report at 64.

Reinsurers outside the United States account for at least 25-31% of all reinsurance in the United States. Freedman, *Reinsurers and Insurers Are Two Peas from Different Pods,* Best's Insurance Management Reports, Property/ Casualty, Release No. 5 (Feb. 22, 1988). Of the one hundred largest reinsurers in the world, only twenty-seven are American

companies. *The World's Top 100 Reinsurers*, ReActions (Mar. 1, 1990) at 13-29. Ninety-seven of these reinsurers are located, however, in countries that have adhered to the Convention.

Many of these reinsurers are now defendants in contract actions commenced by the liquidators of United States companies. As a result of this Court's decision in *Fidelity & Deposit Co. of Md. v. Pink*, 302 U.S. 224, 228 (1937), *reh'g denied*, 302 U.S. 780 (1938), New York and other states enacted legislation that prevents a ceding insurer from taking any credit for reinsurance unless the reinsurance agreement contains a provision requiring payment by the reinsurer "without diminution because of the insolvency of the ceding insurer." N.Y. Ins. Law § 1308; Ill. Rev. Stat. Ch. 73, para. 785.2; Cal. Ins. Code § 922.2. Liquidators of insolvent ceding insurers

rely on these provisions in reinsurance contracts to insist upon payment by reinsurers while ignoring the contractual, statutory, and treaty rights of reinsurers to arbitrate. *See, e.g., Corcoran v. AIG Multi-Line Syndicate, Inc.*, 143 Misc. 2d 62, 539 N.Y.S.2d 630 (Sup. Ct. 1989), *rev'd*, 562 N.Y.S.2d 933 (1st Dep't 1990).

AIG Multi-Line involved twenty-one reinsurers, including seven Bermudan companies. The trial court held that under the Convention the Liquidator's contract action must be arbitrated. 539 N.Y.S.2d at 637. The New York Supreme Court, Appellate Division-First Department, relying on its earlier ruling in this case, reversed and remanded the matter for trial. *AIG Multi-Line* is representative of other actions pending in American courts against reinsurers

located in nations that have adhered to the Convention.

Arbitration is the norm in resolving reinsurance disputes and reinsurance agreements "invariably . . . provide for arbitration of disputes between parties through arbitration." R. Reinarz, *Property and Liability Reinsurance Management* 49 (1969); K. Thompson, *Reinsurance* 140 (4th ed. 1966); *see* 1 K. Gerathewohl, *supra*, at 528. The New York State Court of Appeals itself recognizes this. *Sumitomo Marine & Fire Ins. Co. v. Cologne Reinsurance Co. of Am.*, 75 N.Y.2d 295, 298, 552 N.Y.S.2d 891, 892, 552 N.E.2d 139 (1990).

It must be particularly difficult for reinsurers located in countries that have adhered to the Convention to fathom how their customarily arbitrated contract claims are not arbitrable under the Convention, when it is well known that

even statutory claims of American citizens, ordinarily not arbitrable in the United States, have been consistently referred to arbitration under the same Convention.

It is important that the order below be reviewed and reversed before it not only disrupts the reinsurance and insurance communities, but leads to retaliatory actions against other representatives of the American business community as well.

CONCLUSION

For the foregoing reasons, a writ of certiorari should be granted.

Respectfully submitted,

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April 9, 1991

APPENDIX

State of New York
Court of Appeals
No. 266

James P. Corcoran, Superintendent of Insurance of the State of New York, &c.,

Respondent,

v.

Ardra Insurance Company, Ltd., et al.,

Appellants.

James Veach and Eugene A. Leiman, NY City, for appellants.
William F. Costigan and Patricia A. Griffin, NY City, for respondent.

SIMONS, J:

The issue presented is whether plaintiff, the State Superintendent of Insurance acting as liquidator of an insolvent insurance company, can be compelled to arbitrate the insolvent's claims against a foreign reinsurer. It arises because defendant Ardra Insurance Company, Ltd., a Bermuda reinsurance corporation, and its principals seek to compel plaintiff to arbitrate Ardra's liability to the insolvent, Nassau

Insurance Company, for reinsurance proceeds allegedly due pursuant to three international reinsurance agreements containing arbitration clauses. Defendants claim that the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (Convention) supersedes article 74 of the New York Insurance Law, which authorizes the Superintendent to sue on behalf of insolvent insurance companies, and requires the Superintendent to arbitrate with Ardra on Nassau's behalf. We conclude that the Convention, as a United States treaty, preempts conflicting Federal and State law, but that it excepts the Superintendent from arbitration in this case and allows him to proceed against Ardra in the main action. Accordingly, we affirm the order of the Appellate Division.

I

Nassau Insurance Company was a New York corporation licensed by the Superintendent to conduct insurance business in New York. It was owned by defendants Jeanne S. DiLoreto and Richard A. DiLoreto, its president. In 1976, the DiLoretos established defendant Ardra Insurance Company, Ltd., a foreign reinsurance corporation under their exclusive ownership, which had its principal and only place of business in Hamilton, Bermuda. Jeanne DiLoreto served as president of Ardra. Between 1978 and 1982, Nassau and Ardra entered into three international reinsurance agreements. The agreements covered policies written by Nassau concerning commercial automobile liability, general liability, lawyers professional package liability, excess liability and personal injury protection benefits written under

New York Automobile Statutory No-Fault coverage. Pursuant to the contracts, Ardra assumed a substantial portion of the risk insured in each policy written by Nassau and in consideration Nassau paid Ardra $10,682,924.84 in reinsurance premiums. Each agreement contained a broad arbitration clause requiring extra-judicial resolution of any dispute between Nassau and Ardra.

Nassau subsequently became insolvent and, after efforts to rehabilitate the company failed, the Superintendent commenced a liquidation proceeding pursuant to article 74 of the Insurance Law. In June 1984, Supreme Court appointed plaintiff liquidator and authorized him to take various actions to wind up Nassau's affairs, including taking possession of property, collecting outstanding debts, paying claims arising under policies issued by Nassau,

collecting reinsurance on those claims, and commencing necessary proceedings. Nassau's corporate charter was forfeited and the company was dissolved.

Plaintiff entered in his duties and began to settle claims on Nassau policies. Ardra paid plaintiff reinsurance proceeds due on some of these claims but stopped doing so in February 1985. At that time, Richard DiLoreto sent a letter to the Superintendent stating that Ardra was repudiating the reinsurance agreements with Nassau because the Superintendent refused to allow Ardra's representatives to participate directly in court proceedings involving third-party claims against Nassau's insureds. In response, the Superintendent commenced this action seeking reinsurance balances allegedly owed by Ardra to Nassau and damages from the DiLoretos resulting from their

purported use of "shell" corporations such as Ardra to obstruct recovery on Nassau's obligations to its creditors and insureds. Defendants moved to dismiss the complaint and compel arbitration under the terms of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (June 10, 1958, 21 U.S.T. 2517, T.I.A.S. No. 6997), a United States treaty, and provisions of the Federal Arbitration Act implementing it (9 USC § 201 *et seq.* 208).[1]

Supreme Court denied the motion, holding that the McCarran-Ferguson Act (15 USC § 1011 *et seq.*) which specifi-

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[1] Defendants removed the action to federal court but the United States District Court for the Southern District of New York remanded the action to Supreme Court, holding that abstentation principles required that the New York courts be provided an opportunity to rule on whether the UN Convention preempts the New York Insurance Law and requires the Superintendent to arbitrate with Ardra (*Corcoran v Ardra Insurance Co., Ltd.*, 657 F Supp 1223, *appeal dismissed and petition denied* 842 F2d 31).

cally permits states to regulate insurance companies, insulates plaintiff from the requirements of the Convention and the Federal Arbitration Act.[2] The Appellate Division affirmed, holding that arbitration was not required because various exceptions in the Convention exempted the Superintendent from its provisions.

II

The threshold question is preemption. The Supremacy Clause provides that "all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land" (US Const, Art. VI, § 2). Any Federal or State law that

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[2] The relevant provision of the McCarran-Ferguson Act provides:

> "No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance * * * unless such Act specifically relates to the business of insurance" (15 USC § 1012[b]).

"prevents the Federal Government from 'speaking with one voice' in international trade" must bow to superior authority (*Japan Line, Ltd. v County of Los Angeles*, 441 US 434, 453-454; *see also, Mitsubishi Motors v Soler-Chrysler-Plymouth*, 473 US 614, 631; *Zschernig v Miller*, 389 US 429, 441). If the Convention requires arbitration, it preempts provision of the McCarran-Ferguson Act (*supra*), the Federal Arbitration Act (*supra*) and the State Insurance Law empowering the Superintendent to litigate on behalf of an insolvent insurance company (*see, Cooper v Ateliers De La Motobecane, S.A.*, 57 NY2d 408, 411-412 [proceeding to obtain attachment order prior to arbitration of dispute arising out of international agreement violates Convention]). The focus, therefore, must be on the Convention, not the Federal statutes.

We conclude that the Superintendent, in his capacity as statutory liquidator of Nassau, is exempt from arbitration by exceptions contained in the Convention, that defendants' motion to dismiss was properly denied, and that he may proceed in this action against Ardra to recover on the reinsurance agreements.

III

In 1958, forty-five nations convened the Convention in New York under the auspices of the United Nations to resolve difficulties in existing international agreements and private law to facilitate international arbitration. Resolution was important not only to secure the several advantages available in domestic arbitration -- speed, informality, economy, expertise of decisionmakers (*see generally, Matter of Sablosky v Gordon Co.*, 73 NY2d 133, 138) -- but more importantly to enact uniform standards

for the enforcement of such contracts thus minimizing uncertainties in dealing with unfamiliar laws in several foreign jurisdictions (*see, Scherk v Alberto-Culver Co.*, 417 US 506, 520, n 15; *Cooper v Ateliers De La Motobecane, S.A.*, 57 NY2d at 410, *supra*; Quigley, *Accession by the United States to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards*, 70 Yale L.J. 1049, 1051). To this end, the Convention provides that the courts of acceding nations must recognize arbitration clauses contained in international commercial agreements and the resulting arbitral awards (United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, *supra*, Art. II, ¶ 1, Art. 3, 21 U.S.T. at 2519).

Although the United States attended and participated in the 1958 conference,

it did not sign the treaty. The United States Senate gave its advice and consent to ratification ten years later, in October 1968, and accession was delayed until enactment of amendments to the Federal Arbitration Act implementing the Convention in 1970 (9 USC § 201 *et seq.* 208; *see*, McMahon, *Implementation of the UN Convention on Foreign Arbitral Awards in the U.S.*, 26 Arb. J. 65, 67). In acceding to the Convention, the Senate restricted the treaty's application to commercial matters (*see*, 9 USC § 202; *Mitsubishi Motors v Soler Chrysler -Plymouth*, 473 US 614, 639, n. 21, *supra*).

Plaintiff's first contention is that this limitation bars arbitration of the present dispute because he is acting as a fiduciary, implementing a statutory regulatory scheme at the direction of the court, and that his activities do not

constitute "commercial" matters (*see, Matter of Knickerbocker Agency [Holz]*, 4 NY2d 245, 251). The commercial nature of the relationship is determined at the inception of the agreement, however, not at the time of enforcement and there can be little doubt that the original agreement between Nassau and Ardra arose "out of a legal relationship...considered as commercial" under domestic law (9 USC § 202; *see, Island Territory of Curacao v Solitron Devices, Inc.*, 356 F Supp 1, 13, *affd* 489 F2d 1313).

Although the reinsurance agreements fall within the general scope of the Convention, it is apparent that the drafters did not intend to compel arbitration in all cases involving international commercial disputes because the Convention excepts certain contracts from its terms. As Secretary of State Katzenbach noted in recommending

accession to President Johnson and the Senate, these exceptions "provide substantial safeguards to American citizens against any misuse of the arbitration process" (Senate Doc E, 90th Cong., 2d Sess., at 4 [1968]).

The exceptions relevant to this case are found in Article II of the Convention. They require recognition of an arbitral agreement only when it "concern[s] a subject matter capable of settlement by arbitration" and provide that the court of an acceding nation may refuse to refer disputing parties to arbitration if the international agreement "is null and void, inoperative or incapable of being performed" (United Nations Convention, Art. II, ¶¶ 1, 3, 21 U.S.T. at 2519, *supra*). These exceptions are implemented by examining the domestic law of an acceding nation (*see, Mitsubishi Motors Corp. v Soler Chrysler-*

Plymouth, Inc., 473 US at 639, n. 21, *supra*; *see also*, *Quigley*, *supra*, at 1064; Contini, *International Commercial Arbitration: The United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards*, 8 Am J Comp L 283, 296; Smith, A-National Arbitration, 63 Tul L Rev 629, 631). In the United States statutes provide that insurance is generally a matter of State concern and that the laws of the individual states govern (McCarran-Ferguson Act, 15 USC §§ 1011, 1012[b], *supra*; *see also*, The Bankruptcy Act, 11 USC § 109[b][2] [which exempts insurance companies from its provisions]). Thus, in this case, the law to be applied in interpreting the exceptions is Article 74 of the New York Insurance Law.

As a result of Nassau's insolvency, and plaintiff's substitution to liquidate its assets, the contractual parties and

their relationship have changed. Nassau no longer exists. Plaintiff steps into its shoes, in the sense that he succeeds to its property, but he is a fiduciary, appointed by the court, subject to its exclusive jurisdiction and possessing only the powers authorized by the Legislature (*see*, Insurance Law art. 74). He holds office as liquidator solely to protect the interests of policyholders, stockholders and the public and has no authority to pursue the commercial interests which motivated the original parties to conclude the reinsurance agreements (Insurance Law § 7417; *see*, *Matter of Knickerbocker Agency [Holz]*, 4 NY2d 245, 250, *supra*).

Although the Legislature has granted the Superintendent plenary powers to manage the affairs of the insolvent and to marshal and disburse its assets, the statutory scheme does not authorize his

participation in arbitration proceedings. Over 30 years ago this Court held, when examining an earlier version of the Insurance Law, that absent express authority to do so the Superintendent could not engage in arbitration when acting as a liquidator (*see*, *Matter of Knickerbocker Agency [Holz]*, *supra*, at 251-253). Despite that ruling and periodic amendments to the Insurance Law, the Legislature has not granted the Superintendent the authority to arbitrate disputes and under the statute's provisions, the subject matter of the claims against Ardra must be litigated in Supreme Court. The arbitration clause is "incapable of being performed" (United Nations Convention, Art. II, ¶ 2, *supra*), therefore, and the claims are not "capable of settlement by arbitration" (*id*. Art. I, ¶ 1) under the applicable domestic law.

This interpretation is also supported by Article V of the Convention which specifies when arbitral awards may be denied recognition. It provides that an award need not be enforced if "the subject matter of the difference is not capable of settlement by arbitration under the law of that country [where recognition and enforcement are sought]" (*id.* Art. V, ¶ 2[a]). The practical result of the parallel provisions contained in Articles II and V is to relieve the parties from having to proceed through a futile arbitration in which the resulting award would be unenforceable in New York because of the Supreme Court's exclusive jurisdiction in liquidation matters (*see, Matter of Knickerbocker Agency [Holz]*, 4 NY2d 245, *supra*).

These exceptions are properly construed to effect New York's strong

public policy concerns by maintaining Supreme Court's exclusive jurisdiction over liquidation proceedings. Arbitrators are private individuals, selected by the contracting parties to resolve matters important only to them. They have no public responsibility and they should not be in a position to decide matters affecting insureds and third party claimants after the contracting party has failed to do so. Resolution of such disputes is a matter solely for the Superintendent, subject to judicial oversight, acting in the public interest.

IV

We recognize strong policy concerns of international comity which enjoin us to enforce arbitration agreements when the Convention requires it (*see, Mitsubishi Motors Corp. v Soler-Chrysler-Plymouth, Inc.*, 473 US 614, 629, *supra*; *Scherk v Alberto-Culver Co.*, 417

US at 516-517, *supra*). Moreover, it is the policy in New York to encourage resolution of disputes through arbitration, particularly conflicts arising in the context of international commercial transactions (*see*, *Cooper v Ateliers De La Motobecane, S.A.*, 57 NY2d at 411, *supra*).

The underlying concerns of the Convention are not implicated here, however. The DiLoretos were the principals of Ardra and Nassau and both companies were wholly owned by them. Nassau and the DiLoretos were New York residents and were amenable to process in New York, both personally and by designation of a New York agent to receive process, and the contracts specifically referred to New York law in various clauses. Under the circumstances, the parties had reason to anticipate at the time the contracts were

executed that New York law applied to them and to know from established precedent that arbitration was not an authorized remedy under Article 74 of the Insurance Law in the event of Nassau's insolvency (*Matter of Knickerbocker, supra*). Thus, the case does not present an international merchant subjected to unfamiliar judicial proceedings and the vagaries of foreign law requiring us to exercise a "sensitivity to the need of the international commercial system for predictability in the resolution of disputes" (*Mitsubishi Motors Corp. v Soler-Chrysler-Plymouth, Inc.*, 473 US at 629, *supra*; *see, Cooper v Ateliers De La Motobecane, S.A.*, 57 NY2d at 410-411, *supra*).

We conclude, therefore, that although the reinsurance agreements fell within the broad terms of the Convention, plaintiff is excepted from arbitration

because the arbitration clause and the dispute alleged to be subject to it are not capable of performance and settlement under the law of New York.

Accordingly, the order of the Appellate Division should be affirmed, with costs.

* *

Order affirmed, with costs. Opinion by Judges Simons. Chief Judge Wachtler and Judges Kaye, Alexander, Titone, Hancock, and Bellacosa concur.

Decided December 20, 1990.

SUPREME COURT, APPELLATE DIVISION

First Department, December 1989

Theordore R. Kupferman, J.P.
Sidney H. Asch
E. Leo Milonas
Richard W. Wallach
Israel Rubin, JJ.

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James P. CORCORAN, Superintendent of Insurance of the State of New York, and his successors in office as Superintendent of Insurance of the State of New York, as Liquidator of Nassau Insurance Company, in Liquidation,

Plaintiff-Respondent,

against

ARDRA INSURANCE COMPANY, LTD., Richard A. DiLoreto and Jeanne S. DiLoreto,

Defendants-Appellants.

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No. 38597-98
April 10, 1990

Defendants-appellants appeal from an order of the Supreme Court, New York County (Bruce McM. Wright, J.), entered August 11, 1988 which, *inter alia*, denied their motion to dismiss complaint, and from an order of said court entered on December 7, 1988, which denied their motion for reargument and renewal.

William F. Costigan, of counsel (Anderson Costigan, attorney) for plaintiff-respondent.

James D. Veach, of counsel (Eugene A. Leiman and Jeffrey S. Weinstein with him on the brief; Mound, Cotton & Wollan, attorneys) for defendants-appellants.

ASCH, J.

This action arises from three reinsurance contracts entered into by the now-insolvent Nassau Insurance Company ("Nassau") with the defendant Ardra Insurance Company, Ltd. ("Ardra"), a Bermuda corporation. Defendants Richard A. and Jeanne S. DiLoreto owned and dominated a network of companies including Nassau and Ardra.

The plaintiff Superintendent of Insurance, as Liquidator of Nassau, seeks reinsurance balances allegedly owed by Ardra to Nassau and damages from the individual defendants allegedly resulting from their use of "shell" corporations, including Ardra, in order to obstruct

plaintiff from recovering amounts due under the Reinsurance Agreements.

There was a broad arbitration clause in each of the three Reinsurance Contracts. After the action was started, the defendants invoked the removal jurisdiction of the federal court, seeking to compel the plaintiff Superintendent to arbitrate the dispute under the terms of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, U.S.T. 2517, T.I.A.S. No. 6992, 330 UNTA 38 (1958) (effective December 29, 1970) (the "Convention"), which is implemented as a chapter of the Federal Arbitration Act, 9 USC § 201 *et seq.* (the "FAA"). The District Court remanded the case on federal abstention grounds (*Corcoran v Ardra Ins. Co., Ltd.*, 657 F Supp 1223 at 1236, *affd* 842 F2d 31).

Defendants moved in the State Supreme Court, after the remand, to dismiss the causes of action against Ardra on the ground, *inter alia*, that arbitration was required. The plaintiff cross-moved for summary judgment and the IAS court denied both motion and cross motion. Thereafter, a motion by defendants for renewal and reargument was also denied by the court.

The ultimate issue presented to us is whether the Convention on the Recognition and Enforcement of Foreign Arbitral Awards mandates arbitration of the dispute with defendant Ardra, a Bermuda corporation, by the Superintendent of Insurance as Liquidator, precluding application of the liquidation provisions of the Insurance Law giving the Supreme Court exclusive jurisdiction of claims for and against the insolvent insurer.

The Court of Appeals, in *Matter of Knickerbocker Agency* [Holz] (4 NY2d 245), held that the provisions of the Insurance Law relating to the liquidation of insolvent insurers (now Art. 74) furnishes a comprehensive method for winding up their affairs and that the Supreme Court with the agency of the Superintendent of Insurance is intended by the statute to have exclusive jurisdiction of all claims involving such insolvent insurers (*id.*, at 250). The court found that in keeping with the overall scheme and plan of the statute, the Supreme Court may not be ousted from its jurisdiction in favor of an arbitrative tribunal (p 252). With the onset of insolvency and liquidation, the provisions of the Insurance Law come into effect and any contractual provisions relating to arbitration become of "no effect" (*id.*, at 251).

The invocation of the Federal Arbitration Act (9 USC § 1 *et seq.*) does not require a different result. The McCarran-Ferguson Act (15 USC § 1011 *et seq.*) specifically provides, in pertinent part: "No Act of Congress shall be construed to invalidate, impair or supersede any law enacted by any State for the purpose of regulating the business of insurance ... unless such Act specifically relates to the business of insurance" (15 USC § 1012[b]). Certainly, the liquidation provisions of the Insurance Law were enacted "for the purpose of regulating the business of insurance" (*see, S.E.C. v National Securities, Inc., et al.*, 393 US 453; *Levy v Lewis*, 635 F2d 960) and thus, in accord with McCarran-Ferguson, are not invalidated or impaired by the provisions of the Federal Arbitration Act (*see, Washburn v Corcoran*, 643 F Supp 554).

However, the question remains as to the applicability of the Convention in view of the fact that Ardra is a Bermuda corporation. Defendant Ardra asserts that the Convention supersedes any contrary State policy or statute pursuant to the United States Constitution, article VI, clause 2, citing *Mitsubishi Motors Corp. v Soler Chrysler-Plymouth, Inc.* (473 US 614), where the Supreme Court said:

> [C]oncerns of international comity, respect for the capacities of foreign and transnational tribunals, and sensitivity to the need of the international commercial system for predictability in the resolution of disputes require that we enforce the parties' agreement, even assuming that a contrary result would be forthcoming in a domestic context (*id.*, at 629).

Article V(2)(b) of the Convention provides that enforcement may be refused if doing so would violate the public policy of the enforcing state. While not entirely free from doubt as to the facts

in this case, it has previously been held that this public policy defense is to be narrowly construed (*Schenck v Alberto-Culver Co.* 417 US 506) and must implicate "the forum state's most basic notions of morality and justice" (*Parsons & Whittemore Overseas Co. v Societe General de L'Industrie du Papier*, 508 F2d 969, 974). We assume, arguendo, that this strict standard has not been met here.

However, the Convention, pursuant to article II, paragraph 3, also provides that the matter need not be referred to arbitration if the court finds that the agreement to arbitrate is "null and void, inoperative or incapable of being performed". As noted, the Court of Appeals has held that the insolvency provisions of the Insurance Law vest the Supreme Court with exclusive jurisdiction over the affairs of the insolvent insurer, rendering arbitration clauses

inoperative and non-enforceable against the statutory liquidator (*see, Knickerbocker Agency, Inc. v Holz*, 4 N.Y.2d 245, 251-53).

Defendant Ardra was on notice when it entered into the reinsurance contracts with Nassau that the arbitration provisions of these agreements would become "inoperative" and unenforceable in the event of insolvency. In fact, the agreements provide for payments by Ardra to the Liquidator in the event of Nassau's insolvency.

> Thus, the Reinsurance Agreements appear to contemplate the transformation of the relationship from one of a commercial nature to one of a regulatory nature. The Reinsurance Agreements contain provisions requiring Ardra to pay reinsurance proceeds to the Liquidator of Nassau if Nassau became insolvent. The provisions are modeled upon § 1308 of N.Y.Ins. Law (formerly § 315). The provisions refer expressly to § 315. Thus, it appears that the parties to the Reinsurance Agreements anticipated, under certain circumstances, the application of New York law to their

> relationship. Furthermore, pursuant to the laws of New York, when parties make a contract, it is reasonable to infer that they were aware of relevant law, and those laws "must be deemed to have permeated the agreement and constituted elements of the obligation." *People v Globe Mutual Life Insurance Co.*, 91 N.Y. 174, 179 (1883). This axiom of contract construction has been applied to New York's law of reinsurance and insurer insolvency. [Citations omitted.] Therefore, Ardra must be deemed to have had knowledge, at the time it entered into the contract with Nassau, regarding the exclusive jurisdiction of the State Supreme Court with respect to the liquidation of Nassau, and the probable implications of this jurisdiction for the enforceability of each Reinsurance Agreement's arbitration provisions. (*Corcoran v Ardra Ins. Co., Ltd.*, *supra*, at 1232 n 6.)

Further, as noted by the federal court (*supra*), the relationship between the parties was transformed from "one of a commercial nature to one of a regulatory nature". "In acceding to the Convention, the Senate restricted its applicability to commercial matters, in accord with Art I(3)" (*Mitsubishi Motors*

v Soler Chrysler-Plymouth, supra at 639 n 21.) Since the dispute which arose is not between Ardra and Nassau, but between Ardra and the Superintendent as Liquidator of Nassau, it is not a "commercial" matter. The Liquidator sues Ardra as a fiduciary protecting not only the interests of Nassau, but also policyholders and the general public in the State of New York *(see, Knickerbocker Agency, Inc. v Holz, supra,* at 251; *but cf. Corcoran v AIG Multi-Line Syndicate, Inc.*, ___ Misc2d ___, 539 NYS2d 630, 635).

The Convention also provides that recognition and enforcement of the award may be refused if the award deals with "a difference not contemplated by or not falling within the terms of the submission to arbitration" (art V[1][c]), and if "the subject matter of the difference is not capable of settlement

by arbitration under the laws of that country" (art V[2][a]). In the State of New York, as noted, a "difference" with the Liquidator of an insolvent insurer is not "contemplated" as within an agreement to arbitrate nor "capable of settlement" by arbitration (*see, Knickerbocker Agency, Inc. v Holz, supra*).

Finally, article V(1)(a) authorizes non-enforcement if the parties "were under the law applicable to them, under some incapacity". Although it has been suggested that the incapacity must relate back to the time of contract and intervening liquidation could not, therefore, support a claim of incapacity (*Corcoran v AIG Multi-Line Syndicate, Inc., supra*, at 636):

> [T]he background of the provision suggests that the drafters were concerned with ensuring that both parties be properly represented during the arbitration proceeding; therefore, the provision refers to the parties' capacities at the time

> of arbitration. Moreover, the incapacity determination is to be made "under the law applicable to [the parties]." This provision requires the application of the law of the party's home jurisdiction, as opposed to the law of the state in which the award was made or the law of the underlying contract. In the case of a U.S. party, U.S. law would apply.
>
> The bankruptcy of one of the parties to an arbitration agreement prior to an award falls squarely under this ... exception. ... Since the Convention makes U.S. law applicable with respect to the capacity of U.S. parties, it follows that a bankrupt U.S. party is "under some incapacity" for purposes of determining the enforceability of a post petition arbitral award, and thus such awards should not be enforceable under the Convention as to bankruptcy estate assets.

(Westbrook, *The Coming Encounter: International Arbitration and Bankruptcy*, 67 Minnesota L Rev 595, 614-616).

A fortiori, disputes involving the Liquidator for an insolvent insurer, acting for stockholders, policyholders and the general public, are not arbitrable, since the insolvent insurer

which agreed to arbitrate has come under an incapacity at the time of the arbitration.

Accordingly, the appeal from the order of the Supreme Court, New York County (Bruce McM. Wright, J.), entered August 11, 1988, which, *inter alia*, denied defendants' motion to dismiss the complaint and compel arbitration, should be dismissed as superseded.

Order of the Supreme Court, New York County (Bruce McM. Wright, J.), entered December 7, 1988, which denied defendants' motion for renewal and reargument, should be affirmed, without costs or disbursements.

All concur.

Order filed.

SUPREME COURT OF THE STATE OF NEW YORK - NEW YORK COUNTY - PART 5

PRESENT:
Hon. BRUCE McM. WRIGHT
Justice.

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JAMES CORCORAN

INDEX NO. 9794/85

-against-

ARDA INS. CO.

----------x

MOTION DATE OCTOBER 5, 1988
MOTION SEQUENCE NO. 004

The following papers numbered 1 to ____ read on this motion to renew and reargue

Upon the foregoing papers it is ordered that this motion for renewal and reargument is denied for the reasons expressed in the court's memorandum writing bearing today's date.

DECEMBER 2, 1988

FILED December 7, 1988

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK
----------x

JAMES P. CORCORAN, Superintendent of Insurance of the State of New York, and his successors in office as Superintendents of Insurance of the State of New York, as Liquidator of the Nassau Insurance Company in Liquidation,

Plaintiffs,

-against-

ARDRA INSURANCE COMPANY, LTD., RICHARD A. DiLORETO and JEANNE S. DiLORETO,

Defendants.
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Index No. 9794 - 1985

MOTION #1, OCTOBER 5, 1988

IAS PART 5

BRUCE McM. WRIGHT, J.

The defendants, aggrieved by this court's August 3, 1988 decision and order denying dismissal of the complaint and refusing to compel arbitration, move for renewal and reargument of their motion for that relief. The same decision and order denied to plaintiffs the relief of

summary judgment and their application to punish the defendants for contempt of court.

This matter has been argued in extenso. It has generated a virtual blizzard of paper contention. The issues raised are not those of first impression. Both sides, as well as the court, have briefed the evident and the subtleties. Argument has been heard at great length. The competition of nuance and insistence will not have quiet repose at the level of this assize. The better course, it would seem, is to have an end to Special Term contention and speed this dispute on its way through the appellate courts.

Arguments have been listened to with interest and opposing insights have been noted. No reason is discovered to alter the court's earlier conclusion and renewal and reargument are denied.

Dated: December 2, 1988

SUPREME COURT OF THE STATE OF NEW YORK,
INDIVIDUAL ASSIGNMENT PART 5
at the Courthouse thereof, 60 Centre Street, New York, New York, 10007.

Present:
Hon. BRUCE McM. WRIGHT
Justice.

----------x

JAMES P. CORCORAN, Superintendent of Insurance of the State of New York, et al

Plaintiffs,

-against-

ARDRA INSURANCE COMPANY, LTD., RICHARD A. DiLORETO and JEANNE S. DiLORETO,

Defendants.

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No. ___ on Calendar of MARCH 16, 1988

Upon the foregoing papers this motion by defendant for an order dismissing the complaint and compelling arbitration; the cross-motion by plaintiff for summary judgment, and the motion by plaintiff to punish defendants for contempt, are all decided in accordance with the accompanying memorandum decision.

Dated AUGUST 3, 1988

FILED August 11, 1988

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK
----------x
JAMES P. CORCORAN, Superintendent of Insurance of the State New York,

Plaintiff,

-against-

ARDRA INSURANCE COMPANY, LTD., RICHARD A. DILORETO, and JEANNE S. DILORETO,

Defendants.
----------x

Index No. 9794/85
MOTION MARCH 16, 1988
IAS PART 5

BRUCE McM. WRIGHT, J.

Defendants' motion for an order dismissing the complaint and compelling arbitration; plaintiff's cross-motion for an order granting summary judgment in favor of plaintiff, and plaintiff's motion for an order punishing defendants for contempt, are decided as follows:

The complaint states that Nassau Insurance Co. is a New York casualty insurance corporation and that Ardra is a

Bermuda corporation in the business of reinsuring casualty risks. Ardra is not licensed to do business as an insurer in New York State (Complaint, ¶3).

By Order of Liquidation issued by this court in June, 1984, plaintiff James Corcoran was appointed liquidator to take possession of all property, contracts and rights of action of Nassau Insurance Co., and Nassau was enjoined from transacting any further business. The complaint alleges that "[a]mong the property, contracts and rights of action of Nassau vested with the plaintiff by the Order of Liquidation are reinsurance proceeds due from Ardra pursuant to three Reinsurance Agreements ... entered into by Ardra and Nassau." (Complaint, ¶9). By this action, plaintiffs seeks to recover the proceeds of certain reinsurance agreements between Nassau and Ardra; damages for the costs and disbursements of

recovering those proceeds due to Nassau under the insurance agreements; specific performance of the reinsurance agreements for all amounts which shall become due to Nassau under the reinsurance agreements, or, as an alternative, the posting of letters of credit by Ardra to secure amounts that shall become due to Nassau under the agreements.

Ardra has demanded arbitration of this dispute pursuant to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, December 29, 1970, 21 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.A. (Convention), as implemented by 9 U.S.C. § 201, et seq. (The Federal Arbitration Act). Ardra also asserts that all three treaties between Ardra and Nassau mandate arbitration of all disputes arising out of those treaties. The broad arbitration

clause, contained in all three reinsurance agreements, provides as follows:

> If any dispute shall arise between the Reinsured and the Reinsurer either before or after the termination of this contract, with reference to the interpretation of this contract or the rights of either party with respect to any transactions under this contract, the dispute shall be referred to [arbitration] ...
>
> [Complaint, Exhibits A, B & C, Art. XVI]

The Federal Arbitration Act provides, in pertinent part:

> A written provision in any Maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration any existing controversy rising out of such contract, transaction, or refusal, shall be valid, irrevocable and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.
>
> [9 U.S.C. §2]

Based upon the arbitration clauses contained in the treaties as well as the

Federal Arbitration Act, defendants demand arbitration of the instant dispute.

Plaintiff takes the position that the Superintendent of Insurance, as Liquidator of Nassau, cannot be forced to arbitrate with Ardra because the McCarran-Ferguson Act (15 U.S.C. ¶1011 et seq) insulates state laws governing insurance company liquidation proceedings from application of the Federal Arbitration Act. The McCarran Ferguson Act provides, in pertinent part:

> (a) State regulation. The business of insurance and every person engaged therein shall be subject to the laws of the several states which relate to the regulation or taxation of such business.
>
> (b) Federal regulation. No Act of Congress shall be construed to invalidate, impair or supersede any law enactd by any State for the purpose of regulating the business of insurance ... unless such Act specifically relates the business of insurance.

[15 U.S.C. §1012(a)(b)]

Plaintiff reasons that Art. 74 of the Insurance Law, which regulates, *inter alia*, the liquidation of insurers, was enacted by New York State "for the purpose of regulating the business of insurance" (15 U.S.C. §1012(b)), that the Supreme Court of this State has exclusive jurisdiction of a liquidation proceeding, and that since the Federal Arbitration Act does *not* "specifically relate to the business of insurance" (15 U.S.C. §1012(b)), the Federal Arbitration Act does not apply to this liquidation proceeding. Plaintiff concludes that the McCarran-Ferguson Act insulates him from the arbitration clauses contained in the reinsurance agreements, because the McCarran-Ferguson Act insulates him from the Federal Arbitration Act which provides that such agreements are valid and enforceable (see 9 U.S.C. §§2, 201).

Defendants urge here that the arbitration clauses in the reinsurance agreements must be honored by plaintiff, and that the policy in New York, as expressed by the Court of Appeals, is to "encourage the use of arbitration," particularly "in the context of international trade" (*Cooper v Ateliers de la Motobeane*, 57 NY 2d 408, 411). Defendants point out that plaintiff has never expressed any reason for refusing to arbitrate the disputed claims with defendants, and that arbitration is clearly the most expeditious method for resolving their dispute.

Among the cases cited by defendants in support of their request that this court issue an order compelling arbitration are *Bernstein v Centaur Insurance Company*, 606 F. Supp. 98 (S.D.N.Y. 1984) and *Gordon v United States Department of Treasury*, 668 F. Supp. 483 (D.Md. 1987),

aff'd 846 F. 2d 272 (1988). In *Bernstein supra*, the district court held that arbitration was not precluded by the McCarran-Ferguson Act. The court stated:

> In summary, no state law explicitly precludes arbitration of insurance cases *and the case law inferring such a rule does so with reference to cases brought within the jurisdiction of the state Supreme Court. Because this case is not within the exclusive jurisdiction of the state Supreme Court and is not one brought under article XVI of the New York Insurance Law, it is not governed by Knickerbocker.* It may be that New York's policy against arbitrating this kind of suit weighs against enforcement of the arbitration clause, but the McCarran-Ferguson Act exempts state practices from preemption only if a state's law would be invalidated, impaired, or superseded. See 15 U.S.C. § 1012)(b). It does not stretch the exception to include state policies for which no specific law is enacted. See *Miller v National Fidelity Life Ins. Co.*, 588 F.2d 185, 187 (5th Cir. 1979) (state regulations of insurance business generally do not trigger McCarran-Ferguson Act where no specific state law would be impaired, invalidated or superseded). (emphasis supplied)
>
> [606 F. Supp 98, 103]

In *Gordon, supra*, the United States Court of Appeals for the Fourth Circuit affirmed the Maryland District Court's finding that "... the liquidation of an insolvent insurance company and the priority of claims paid thereto does not constitute the "business of insurance" as that term is used in the McCarran-Ferguson Act." (668 F. Supp. at p. 491)

The holding in *Bernstein v Centaur Insurance Co.* (606 F. Supp 98) was addressed by Mr. Justice Ira Gammerman in his decision in *Matter of Union Indemnity Insurance Company of NY* (137 Misc. 2d 575), cited by plaintiff here. In that case, Justice Gammerman denied a motion by reinsurers to compel the Liquidator to arbitrate claims pursuant to arbitration clauses contained in the reinsurance agreements. Presented with many of the same arguments that are raised here, the court concluded that arbitration was not

available to resolve the dispute between the reinsured and the reinsurers once liquidation proceedings had been commenced, and that "[t]he resolution of all claims for or against the insolvent carrier must proceed before the liquidation court. (citation omitted)". (137 Misc. 2d at p 581). Mr. Justice David Edwards, Jr. of this court applied similar reasoning in *Corcoran v Doug Ruedlinger, Inc* (Index No. 5349/87, slip op. 8/21/87), when he denied a motion to compel the liquidator to proceed to arbitration, finding that the McCarran-Ferguson Act "... excludes application of the FAA thereby protecting Article 74 of the State Insurance Law from federal preemption." (slip op., p. 5).

In *Matter of Union Indemnity Ins. Co. supra*, the holding in *Bernstein* was distinguished on the basis that the *Bernstein* court had "... concluded that

since the Superintendent of Insurance had become a plaintiff in the Federal court the "case is not within the exclusive jurisdiction of the state Supreme Court and is not brought under Article XVI [now Art. 74] of the New York Insurance Law" (606 F Supp, at 103), and, therefore, "not governed by *Knickerbocker*." (137 Misc. 2d 575). Here, as in *Matter of Union Indemnity Insurance Co. supra*, the plaintiff has not sued in Federal court.

In *Matter of Knickerbocker Agency* (Holz), 4 NY 2d 245, also cited by Mr. Justice Gammerman in *Matter of Union Indemnity Insurance Co., supra*, the Court of Appeals denied a motion to compel arbitration made by an alleged debtor of an insurance company in liquidation and held that the Supreme Court is the exclusive forum for resolution of a claim by a liquidator against a debtor who was a resident of New York State. The

Knickerbocker court expressly stated that it was not concerned with nonresidents, as are defendants in this case. However, Mr. Justice Gammerman implicitly extended the holding in *Knickerbocker* to claims against nonresident reinsurers, as the case before him involved nonresident reinsurers.

In *Washburn v Corcoran*, 643 F. Supp. 554 (S.D.N.Y. 1986), also cited with approval in *Matter of Union Indemnity Insurance Co.*, *supra*, the District Court (Leval, J.) denied a motion to compel arbitration of a reinsurance contract dispute. Judge Leval noted:

> Article 74 [of the New York Insurance Law] requires that the liquidation of an insurance compa.., be conducted within the jurisdiction of the New York court. See §7417, 7403, 7405, 7409, 7432, 7434. The highest court of New York made clear in *Knickerbocker* that this grant of jurisdiction was exclusive and further required that all proceedings in liquidation be unified under the "single management of one court" to insure economical,

> efficient and orderly liquidation.
> * * *
>
> [643 F. Supp 554, 556]
>
> The court also wrote:
>
> As the highest court of New York has ruled that arbitration is incompatible with the commands of Article 74, it necessarily follows that enforcement of a federal statute requiring arbitration would defeat this provision of the state statute.
>
> [643 F. Supp. 554, 557]

This court declines to adopt the Fourth Circuit's finding that the liquidation of an insolvent insurance company does not constitute the "business of insurance" as that term is used in the McCarron-Ferguson Act. (see *Gordon, supra*). Based upon the holdings in *Matter of Union Indemnity Ins. Co. supra, Washburn v Corcoran, supra*, and *Corcoran v Doug Ruedlinger, Inc. supra*, this court concludes that defendant's motion for an order dismissing the complaint and compelling arbitration, must be denied.

Plaintiff's cross-motion for summary judgment must also be denied. As a result of defendants' motion to dismiss the complaint and to compel arbitration, as well as plaintiffs' cross-motion for summary judgment, discovery has not been conducted in this action. Defendants have requested an opportunity to conduct discovery, in the event that this court denies their motion to compel arbitration. As noted, that motion has been denied.

Further, triable issues of fact exist, such as whether plaintiff breached the subject treaties by refusing to allow defendant Ardra to be associated with Nassau in the defense of Nassau's claims (Reinsurance Agreements, Art. VII (3)), and whether Ardra's reinsurance exposure was unnecessarily high (i.e. was the Superintendent negligent in handling the claims against Nassau and did the

Superintendent act in good faith towards the reinsurer). Such issues of fact preclude the granting of summary judgment to plaintiff.

Finally, plaintiff's motion for an order punishing defendants for contempt, brought by order to show cause signed on June 5, 1987, is denied without prejudice on the ground that the order was not properly served upon defendants. It appears that the copy of the order to show cause which was served upon defendant Richard DiLoreto (on behalf of all defendants) was not properly conformed to the original in that it did not indicate that it had been signed. Further, the original order to show cause provided for a service date of June 8, 1987, and the Order was not served until June 12th. While plaintiff's counsel states that this court extended the service date to June 17 (Veich letter

dated June 17, 1987) that later date was also not reflected on the copy that was served upon defendants. In view of the foregoing, the order to show cause dated June 5, 1987 is deemed marked off, without prejudice to renewal before the Justice to whom this action now is assigned.

Dated: August 3, 1988

FILED: August 11, 1988

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 256 - August Term 1987

Argued Nov. 16, 1987
Decided March 17, 1988.

Docket 87-7478.

JAMES P. CORCORAN, SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK, AND HIS SUCCESSORS IN OFFICE AS SUPERINTENDENTS OF INSURANCE OF THE STATE OF NEW YORK, AS LIQUIDATOR OF NASSAU INSURANCE COMPANY, IN LIQUIDATION,
Plaintiff-Appellee,

-v.-

ARDRA INSURANCE COMPANY, LTD., RICHARD S. DILORETO, AND JEANNE S. DILORETO,
Defendants-Appellants.

Before KEARSE and ALTIMARI, Circuit Judges, and LASKER, District Judge.*

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* Honorable Morris E. Lasker, Senior Judge of the United States District for the Southern District of New York, sitting by designation.

New York State Superintendent of Insurance, as liquidator of insolvent New York insurer, filed suit in state court against Bermuda reinsurer and two of its officers, seeking to recover reinsurance proceeds. Action was removed. Reinsurer and its officers sought order compelling arbitration and Superintendent sought remand. The United States Districe Court for the Southern District of new York, Peter K. Leisure, J., remanded to state court, and reinsurer and its officers appealed. Superintendent moved to dismiss appeal.

Appeal dismissed; mandamus denied.

John S. Kinzey, New York City (Cecelia Kempler, Ronald J. Gizzi, LeBoeuf, Lamb, Leiby & MacRae, Joseph Termini, Termini & Epstein, New York City, on the brief), for plaintiff-appellee.

James D. Veach, New York City (Eugene A. Leiman, Mound, Cotton & Wollan, New York City, on the brief) for defendants-appellants.

KEARSE, *Circuit Judge*:

Defendants Ardra Insurance Company, Ltd. ("Ardra"), *et al.*, appeal from an order of the United States District Court

for the Southern District of New York, Peter K. Leisure, *Judge*, remanding this action, brought in state court by James P. Corcoran as the Superintendent of Insurance of the State of New York ("Superintendent") to recover proceeds allegedly due under three reinsurance agreements, to state court on grounds of abstention. Ardra contends that abstention was inappropriate because, pursuant to arbitration clauses in the reinsurance agreements, the district court was required to order arbitration of the dispute under the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "Foreign Arbitral Awards Convention" or "Convention"), Dec. 29, 1970, 21 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.A. 38. The Superintendent contends (1) that the appeal should be dismissed pursuant to 28 U.S.C. § 1447(c) and (d)

(1982) for lack of appellate jurisdiction, (2) that the district court properly abstained, and (3) that even if abstention was improper, the case was correctly remanded to state court because the McCarran-Ferguson Act, 15 U.S.C. § 1011 *et seq.* (1982), supersedes the Convention. For the reasons below, we dismiss the appeal for lack of a final order, and, treating the appeal as a petition for mandamus, we deny the petition.

I. BACKGROUND

Ardra is a Bermuda insurer that entered into three reinsurance agreements with a New York insurance company, Nassau Insurance Company ("Nassau"). Nassau has been in liquidation since June 1984, and the Superintendent, as its liquidator, was authorized by an Order of Liquidation, issued pursuant to Article 74 of the New York Insurance Code, N.Y.

Ins. Law § 7401 *et seq.* (McKinney 1985), to pay claims arising under policies issued by Nassau and to collect reinsurance on such claims. The Superintendent sought reinsurance payments from Ardra, which repudiated its obligation to make such payments, on the ground that the Superintendent had refused to allow Ardra's representatives to participate in court proceedings involving third-party claims against Nassau's insureds. The Superintendent commenced the present action against Ardra and two of its officers in New York State Supreme Court to recover the reinsurance payments.

Defendants responded by demanding arbitration pursuant to arbitration clauses in the reinsurance agreements and eventually removed the case to the district court pursuant to 9 U.S.C. § 205 (1982), which allows removal of any state

court action relating "to an arbitration agreement or award falling under the Convention." Defendants moved in the district court for an order compelling arbitration, dismissing the complaint against Ardra, and dismissing or staying all proceedings as to the individual defendants. Corcoran moved to remand the case to state court, contending (1) that the McCarran-Ferguson Act gave the state courts exclusive jurisdiction over all matters relating to the liquidation of Nassau, (2) that the Convention was inapplicable to a suit brought by a state official whose recovery powers by law exceeded Nassau's rights under the reinsurance agreements, and (3) that the district court should abstain in order to allow the state court to decide state-law issues of first impression raised by the Superintendent.

In an opinion reported at 657 F. Supp. 1223 (1987), Judge Leisure granted the remand motion. Noting that the Convention applies only to "commercial relationships and disputes arising out of those relationships," *id.* at 1228, the court concluded that the question of whether the Superintendent merely stood in Nassau's shoes or had greater rights than Nassau was a novel question of state law that was of considerable importance to the state's system of regulating insurance liquidations. The court chose to abstain from deciding this issue, which would affect the applicability of the Convention, and it remanded the action to state court. The court noted that it had not decided any of the issues central to the dispute between the parties, such as the merits of the Superintendent's claims for reinsurance proceeds, the interplay between the

Convention and New York's regulatory system or the McCarran-Ferguson Act, or the applicability of the Convention to the present controversy. Rather, the remand left the resolution of all such questions to the state court.

Defendants have appealed, contending that the district court improperly abstained from deciding important questions of federal law. The Superintendent, in addition to defending the merits of the district court's remand decision on essentially the same grounds advanced in support of his remand motion, has moved to dismiss the appeal on the ground that a remand order is not appealable.

II. DISCUSSION

The principal questions before us are whether the district court's remand order is reviewable; if it is reviewable, whether the proper mechanism for review is appeal or mandamus; and, upon review

under the appropriate standard, whether the remand order was proper. We conclude that the district court's order remanding the case is reviewable, but not by appeal. We treat the appeal as a petition for mandamus, and we deny the petition.

A. *The Reviewability of the Remand Decision*

Section 1447(d) of 28 U.S.C. provides, with one exception not pertinent here, that "[a]n order remanding a case to the State court from which it was removed is not reviewable on appeal or otherwise...." 28 U.S.C. § 1447(d). The Supreme Court has interpreted this provision as prohibiting appellate review only with respect to remand orders issued under § 1447(c), which requires the district court to remand a case if it appears, prior to final judgment, that the action "was removed improvidently and

without jurisdiction." 28 U.S.C. § 1447(c); *see Carnegie-Mellon University v. Cohill*, ___ U.S. ___, 108 S.Ct. 614 (1988) ("*Cohill*"); *Thermtron Products, Inc. v. Hermansdorfer*, 423 U.S. 336 (1976) ("*Thermtron*"). If the action is one that was properly removed to the district court, and the district judge bases his remand on some ground other than the ground that the removal was improvident or without jurisdiction, the remand order is reviewable by the court of appeals. *Thermtron*, 423 U.S. at 351; *see generally Cohill*, 108 S.Ct. at 616-22.

Removal in the present case was predicated on the Foreign Arbitral Awards Convention. The Convention deals with arbitration agreements arising out of, *inter alia*, commercial relationships between citizens of the United States and citizens of foreign states. 9 U.S.C.

§ 202 (1982). The procedures enacted by Congress for federal judicial treatment of agreements falling under the Convention are set forth in 9 U.S.C. §§ 201-208 (1982). Section 203 treats an action to enforce an agreement falling under the Convention as one arising under the laws and treaties of the United States and gives the district courts original jurisdiction over such an action. Section 205 provides that where the subject matter of an action pending in a state court relates to an arbitration agreement falling under the Convention, the defendant may, at any time before trial, remove the action to the district court; the ground for removal need not appear on the face of the state court complaint but may be shown in the petition for removal.

In the present case, Ardra moved in state court to compel arbitration on the

ground that the reinsurance agreements between itself, a Bermudan citizen, and Nassau, a citizen of the United States, provided for arbitration. Prior to trial, Ardra removed the case to the district court. In remanding, the district court did not suggest that it lacked jurisdiction or that the action had not been removed in accordance with the prescribed procedures. Rather, it found that the applicability of the Convention would depend on the powers granted by state law to the Superintendent, and, relying principally on *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943) ("*Burford*"), and to an extent on *Colorado River Water Conservation District v. United States*, 424 U.S. 800 (1976) ("*Colorado River*"), it decided to remand as an exercise of its discretion to abstain from the decision of difficult questions of state law. Since the remand

was not based on the grounds provided by 28 U.S.C. § 1447(c), our review of the remand order is not barred by § 1447(d).

Nonetheless, we are compelled to conclude that Ardra's appeal from the remand order must be dismissed, for *Thermtron* makes clear that the proper vehicle for review of a remand order is mandamus, not appeal: "[B]ecause an order remanding a removed action does not represent a final judgment reviewable by appeal, '[t]he remedy in such a case is by mandamus, to compel action, and not by writ of error to review what has been done.'" 423 U.S. at 352-53 (quoting *Railroad Co. v. Wiswall*, 90 U.S. (23 Wall.) 507, 508 (1875)). We note that some orders that ordinarily are not considered final have been deemed final for reasons that would apparently warrant treating remand orders as final. Thus, in *Moses H. Cone Memorial Hospital v.*

Mercury Construction Corp., 460 U.S. 1, 8-10 (1983) ("Moses Cone"), a district court's stay of a diversity action pending resolution of a concurrent state-court action was held to be a final order appealable under 28 U.S.C. § 1291 (1982). The Supreme Court ruled that although "a stay is not ordinarily a final decision for purposes of § 1291, since most stays do not put the plaintiff 'effectively out of court,'" a stay that "*refuses to allow* the plaintiff to litigate his claim in federal court" is final and appealable "when the sole purpose and effect of the stay are precisely to surrender jurisdiction of a federal suit to a state court." *Id.* at 10-11 n. 11 (emphasis in original). Though it is by no means clear why an order that remands an action to state court is any less final than the stay discussed in *Moses Cone*, the ruling in

Thermtron that a remand order is not reviewable by appeal could not have been more explicit. Under the surrender-of-federal-jurisdiction test used in *Moses Cone*, we wonder whether it can logically or prudently remain the rule that a reviewable remand order (*i.e.*, one whose review is not barred by § 1447(d)) is not reviewable by direct appeal. If the district court dismisses an action on grounds that are discretionary, its order may be appealed and may be reversed if it has abused its discretion; yet the effect of denying direct appeal of a reviewable remand order is to insulate the order when the district court (1) has the power to dismiss on a discretionary ground, (2) chooses instead to remand on that ground, and (3) would have abused its discretion in dismissing on that ground, for, as discussed in Part II.B below, mandamus will not issue to remedy an ordinary

abuse of discretion. It is hardly clear to us that such insulation of a reviewable remand order is necessary or sound.

Nonetheless, *Thermtron's* explicit ruling that review must be by mandamus rather than appeal has recently been reinforced by *Cohill*, in which the Third Circuit's review by means of mandamus rather than appeal drew no criticism from the Supreme Court, *see* 108 S.Ct. at 617 & n. 4, in the face of the long established principle that mandamus is not appropriate where a direct appeal would lie, *see, e.g., Helstoski v. Meanor*, 442 U.S. 500, 505-08 (1979); *Ex parte Rowland*, 104 U.S. (14 Otto) 604, 617 (1882). Accordingly, we conclude that the remand order at issue in the present case is not appealable and may be reviewed only by petition for mandamus.

Our recent decision in *Karl Koch Erecting Co. v. New York Convention Center Development Corp.*, 838 F.2d 656 (2d Cir. 1988) ("*Karl Koch*") is not to the contrary. In *Karl Koch*, the district court had remanded because it interpreted a forum-selection provision agreed to by the parties as requiring that the controversy be litigated in state court. We held that "a remand order based on a district court's interpretation of a forum-selection clause is reviewable on appeal," rather, than by mandamus, 838 F.2d at 659 & n. 1, relying on the Ninth Circuit's decision in *Pelleport Investors, Inc. v. Budco Quality Theatres, Inc.*, 741 F.2d 273, 277 (9th Cir. 1984). *Pelleport* upheld appealability on the ground that that part of the district court's remand order which definitively ruled on the validity and meaning of the parties' forum-selection

agreement was a collateral order that was final within the meaning of § 1291 and was appealable under the *Cohen* doctrine, *Cohen v. Beneficial Industrial Loan Corp.*, 337 U.S. 541, 546 (1949). The availability of appeal under the *Cohen* doctrine distinguishes *Karl Koch* from this case. To be appealable under that doctrine, an order must, *inter alia*, "'conclusively determine [a collateral] disputed question.'" *Moses Cone*, 460 U.S. at 11 (quoting *Coopers & Lybrand v. Livesay*, 437 U.S. 463, 468 (1978)). In the present case, unlike *Karl Koch*, there is nothing conclusive about the district court's order. In *Karl Koch*, the collateral dispute was whether the merits of the litigation should be decided in state court or in federal court; the district court, in remanding the matter to state court, conclusively determined that issue. Here, the collateral issue

is whether the matter should be adjudicated by an arbitrator. The district court did not, by remanding to state court, resolve that issue, for if the state court determines that the pertinent powers of the Superintendent are strictly derived from the rights of Nassau, and thus are "commercial," the state court itself will be required, under the Supremacy Clause of the Constitution, to order arbitration pursuant to the Convention. Accordingly, we conclude that the abstention-remand order here is not a final order within the meaning of *Cohen*, and hence, in accordance with *Thermtron* and *Cohill*, is not reviewable by means of appeal.

Although our normal practice is to decline to treat improvident appeal as petitions for mandamus, *see generally Bridge C.A.T. Scan Associates v. Technicare Corp.*, 710 F.2d 940, 944 (2d

Cir. 1983), we believe this case warrants a departure from that practice, for there is a strong public interest in promoting the Superintendent's efficient performance of his official duties. The resolution of the present case, which was removed from state court more than two-and-one-half years ago, has already been unduly delayed. We prefer not to prolong matters further by requiring the parties to file new papers in order to obtain review by means of mandamus. Accordingly, we treat Ardra's appeal as a mandamus petition, and turn to the merits.

B. *The Merits*

Mandamus is an extraordinary writ that has been issued to a federal court only "'to confine an inferior court to a lawful exercise of its prescribed jurisdiction or to compel it to exercise its authority when it is its duty to do so.'"

Will v. United States, 389 U.S. 90, 95 (1967) (quoting *Roche v. Evaporated Milk Association*, 319 U.S. 21, 26 (1943)). The writ is available only when there has been a "'usurpation of judicial power' or a clear abuse of discretion." *Schlagenhauf v. Holder*, 379 U.S. 104, 110 (1964) (quoting *Bankers Life & Casualty Co. v. Holland*, 346 U.S. 379, 383 (1953)). We find no lack of power or abuse of discretion here.

Although *Thermtron*, which dealt with a remand on grounds that were clearly beyond the district court's power, seemed to rule broadly that a district court lacked the power to remand a case to state court for any reason other than one provided in § 1447(c), *see* 423 U.S. at 345 & n. 9 ("cases properly removed from state to federal court within the federal court's jurisdiction may not be remanded for discretionary reasons not authorized

by the controlling statute"); *id.* at 351, *Cohill* reveals that the permissible bases for remand are not so limited. In *Cohill*, an action involving one federal claim and several pendent state-law claims was removed from state court to federal court; when the plaintiffs withdrew the federal claim, the district court remanded the pendent claims to state court. Since the removal had not been improvident or without jurisdiction, this remand was not one provided for by § 1447(c). Nonetheless, the Supreme Court upheld the Third Circuit's denial of the defendants' mandamus petition, ruling that since the district court undoubtedly had the power, once all federal claims were gone, to decline to entertain the suit by dismissing the pendent claims, it had the inherent power to decline by remanding those claims to state court. 108 S.Ct. at 619-21. Since

the removal served the same principles, i.e., "economy, convenience, fairness, and comity," that underlay the court's power to decline to exercise pendent jurisdiction, the *Cohill* Court concluded that remand was not precluded either by § 1447(d) or by *Thermtron*. 108 S.Ct. at 621.

By the same line of reasoning, we conclude that if a district court has the power to dismiss an action on grounds of abstention it has the power to remand to the state court on those grounds. It is plain that in appropriate circumstances the court may dismiss on abstention grounds, *see Burford*, 319 U.S. at 334; *see generally Moses Cone*, 460 U.S. at 15-16; *Colorado River*, 424 U.S. at 817-19, for it is "well settled that a district court is 'under no compulsion to exercise [its] jurisdiction,' .... where the controversy may be settled more

expeditiously in the state court," *Will v. Calvert Fire Insurance Co.*, 437 U.S. 655, 662-63 (1978) (quoting *Brillhart v. Excess Insurance Co.*, 316 U.S. 491, 494 (1942)). The very goals reflected in the principle that the court may dismiss on grounds of abstention persuade us that when the district court has decided not to hear a removed case on grounds of abstention, it need not dismiss but may instead remand. For example, abstention pursuant to *Burford* is designed to avoid federal court interference with specialized ongoing state regulatory schemes, *see* 319 U.S. at 327; a dismissal pursuant to *Colorado River* is designed to promote "'conservation of judicial resources and comprehensive disposition of litigation'" 424 U.S. at 817 (quoting *Kerotest Manufacturing Co. v. C-O-Two Fire Equipment Co.*, 342 U.S. 180, 183 (1952)). All of these goals are likely

to be furthered by remanding a removed action to state court, thereby accommodating the values of economy, convenience, and comity, and avoiding the delay involved in dismissing the federal litigation and requiring the parties to start anew in the very court in which they initially began. Thus, in *Naylor v. Case & McGrath, Inc.*, 585 F.2d 557, 565 (2d Cir. 1978), we stated that "abstention can be exercised through remand, assuring an adjudication of the state law issues in the pending action without risk of delay. That is the indicated course where, as here, the state law is uncertain and its resolution a matter of concern to the state." In sum, we conclude that when the district court may properly abstain from adjudicating a removed case, it has the power to remand the case to state court.

Finally, we conclude that the underlying decision to abstain in the present case was not an abuse of discretion. We have noted that New York's "'complex administrative and judicial system for regulating and liquidating domestic insurance companies'" is the type of regulatory scheme that warrants serious consideration of abstention when the question before the court is a novel one. *Law Enforcement Insurance Co. v. Corcoran*, 807 F.2d 38, 43-44 (2d Cir. 1986) (quoting *Levy v. Lewis*, 635 F.2d 960, 963 (2d Cir. 1980) (abstention appropriate even where novel question involved interplay between insurance law and federal law)), *cert. denied*,___ U.S. ____, 107 S. Ct. 1896 (1987). Under New York law, the Superintendent's power to collect on reinsurance agreements entered into by a liquidated company is a matter

of no little concern, for policy holders have no direct right of action against reinsurers; only the Superintendent, as liquidator, can recover from the reinsurer. *Skandia America Reinsurance Corp. v. Schenk*, 441 F. Supp. 715, 724 (S.D.N.Y. 1977); *see* N.Y. Ins. Law § 7405. The extent to which the Superintendent is able to collect thus affects the degree to which the insolvent insurer's estate will have assets sufficient to satisfy the claims of its creditors. It is clear that these questions are important to the state regulatory scheme and that the scope of the Superintendent's power, insofar as it is pertinent to this case, has not yet been resolved by the state courts. Accordingly, the district court's decision to abstain appears to fit particularly well within the *Burford* goal of avoiding interference with specialized

state regulatory schemes. In all the circumstances, we conclude that there has been no abuse of discretion, much less the clear abuse required to warrant the issuance of mandamus.

CONCLUSION

We have considered all of the arguments advanced by Ardra in support of its challenge to the remand order and have concluded that they are without merit.

The appeal is dismissed; mandamus is denied.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

JAMES P. CORCORAN, Superintendent of Insurance of the State of New York, and his successors in office as Superintendents of Insurance of the State of New York, as Liquidator of Nassau Insurance Company, in Liquidation,
Plaintiff,

v.

ARDRA INSURANCE COMPANY, LTD., Richard S. DiLoreto and Jeanne S. DiLoreto,
Defendants.

No. 85 Civ. 6304 (PKL).

OPINION AND ORDER

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LEISURE, *District Judge*:

Plaintiff, James P. Corcoran, Superintendent of Insurance of the State of New York ("the Superintendent"), as Liquidator of Nassau Insurance Company ("Nassau"), has brought this action against the Ardra Insurance Company Ltd. ("Ardra"), a Bermuda reinsurance company, and two officers of Ardra, Richard S. Diloreto and Jeanne S. Diloreto (the "Diloretos") seeking the recovery of reinsurance proceeds under three reinsurance agreements (the "Reinsurance Agreements") between Nassau and Ardra. The Superintendent commenced this action in New York State Supreme Court, New York County. Subsequently, Ardra demanded

arbitration under each of the Reinsurance Agreements. Pursuant to Ardra's arbitration demands, defendants also moved to dismiss or stay the state action and for relief prior to answer pursuant to N.Y.C.P.L.R. § 3211(a). The Superintendent responded by cross-moving for summary judgment. Instead of replying to the Superintendent's motion in the state court, defendants removed this action to this Court, seeking an order compelling arbitration, dismissing the complaint against Ardra, and dismissing or staying all proceedings with respect to the DiLoretos. In response, the Superintendent seeks remand of this action to the state court. For the reasons set forth below, the Superintendent's motion for remand is granted.

FACTUAL BACKGROUND

In this action, the Superintendent, as Liquidator of Nassau, seeks recovery

of reinsurance[1] proceeds allegedly owed by Ardra to Nassau for payment of claims arising under certain policies issued by Nassau. *See* Complaint at ¶ 1. Specifically, this dispute involves three Reinsurance Agreements entered into by Nassau and Ardra. The Reinsurance Agreements covered (a) commercial automobile liability, general liability, lawyers professional package liability, excess commercial automobile liability and excess general liability policies written by Nassau, (b) personal injury protection benefits written under New York Automobile Statutory No-Fault

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[1] "Reinsurance is the 'ceding by one insurance company to another of all or a portion of its risks for a stipulated portion of the premium, in which the liability of the reinsurer is solely to the . . . ceding company . . . [which] retains all contact with the original insured, and handles all matters prior to and subsequent to loss.'" *Skandia America Reinsurance Corp. v. Schenck*, 441 F. Supp. 715, 724 (S.D.N.Y. 1977) (quoting 13A J. Appelman & J. Appleman, *Insurance Law & Practice* § 7681, ch. 278, at 480 (rev. ed. 1976)).

coverage, and (c) excess automobile bodily injury medallion taxicab policies. *See* Affidavit of Ronald J. Gizzi, Esq., sworn to on August 29, 1985 ("Gizzi Aff."), Exhibits B, C and D, annexed thereto. Ardra assumed a substantial portion of risks on those policies written by Nassau which were covered pursuant to the Reinsurance Agreements. In consideration for Ardra reinsuring such a substantial portion of Nassau's liabilities, Nassau paid $10,682,924.84 in premiums to Ardra.

Nassau was placed in liquidation on June 22, 1984, after having been in rehabilitation for three months. The Order of Liquidation (the "Order") was issued pursuant to Article 74 of the New York Insurance Code, N.Y. Ins. Law § 7401 *et seq.* (McKinney 1985), which governs the manner of rehabilitation and liquidation of insolvent insurers

domiciled in New York, Nassau's state of domicile. The Order authorizes the Superintendent, in his capacity as Liquidator of Nassau, to take various actions, including taking possession of the property of Nassau, liquidating the business of Nassau, paying claims arising under policies issued by Nassau, collecting reinsurance on such claims, and collecting other debts owed to Nassau. The Order also terminates all outstanding policy and other insurance obligations of Nassau, as well as other subsisting contracts, tax sharing agreements and other obligations of Nassau. Finally, the Order prohibits all persons, "including but not limited to claimants", from:

> [B]ringing . . . any action at law, suit in equity, *special or other proceeding* against [Nassau] or its estate, or the Superintendent . . . or from in any way interfering with the Superintendent . . ., in his or their possession, control or manage-

> ment of the property of said corporation, or in the discharge of his or their duties as Liquidator thereof, or in the liquidation of the business of said corporation . . . .

Order of Liquidation at 8 (emphasis added).

On February 19, 1985, Ardra's Board of Directors authorized the sending of a disclaimer letter to the Superintendent. The letter stated that Ardra was repudiating the Reinsurance Agreements because the Superintendent failed to cooperate with Ardra by allowing Ardra's representatives to participate directly in court proceedings involving third party claims against Nassau's insureds as allegedly required under the Reinsurance Agreements. Subsequently the Superintendent commenced this action.

LEGAL DISCUSSION

Defendants argue that this dispute is "basically a contract action brought

by plaintiff as liquidator of Nassau . . . against [Ardra], a Bermuda reinsurance company." D. Memo. at 1. Defendants allege that because the dispute between Ardra and the Superintendent purportedly "falls clearly within mandatory arbitration clauses in each of the reinsurance agreements . . ." the instant matter should be referred to arbitration. *Id.* More specifically, according to defendants, the Court has the power and obligation to refer this dispute to arbitration under the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 21 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.S. 38 (Dec. 29, 1970), *implemented* by 9 U.S.C. § 201 *et seq.* (the "Convention"). The Superintendent, however, contends that this action should be remanded to the State Supreme Court on the grounds that (1) the State Supreme

Court has exclusive jurisdiction over all matters relating to the liquidation of Nassau pursuant to Article 74 of the New York Insurance Code and in accordance with the delegation of powers to the states by the McCarran-Ferguson Act ("McCarran-Ferguson"), 15 U.S.C. § 1011 *et seq.*; (2) the Convention does not apply to the instant dispute; and (3) abstention is appropriate to allow the State Supreme Court to decide issues of first impression raised by the Superintendent. P. Memo. at 1-2.

This Court has confronted previously the issue of whether the McCarran-Ferguson Act precludes the application of the Federal Arbitration Act, 9 U.S.C. § 1 *et seq.* (1976) (the "Arbitration Act") to Article 74. *See Washburn v. Corcoran*, No. 85-2674 (S.D.N.Y. Sept. 22, 1986) (Leval, J.); *Bernstein v. Centaur Ins. Co.*, 606 F. Supp. 98 (S.D.N.Y. 1984).

However, the question now possibly before the Court, regarding the relationship between the Convention and McCarran-Ferguson, is one of first impression.[2] Although this question is undoubtedly significant and interesting, before reaching it the Court must be satisfied first that the Convention applies to this dispute.

A. *THE CONVENTION*

As the Second Circuit explained in *Bergesen v. Joseph Muller Corp.*, 710 F.2d 928 (2d Cir. 1983), "[i]nternational merchants often prefer arbitration over litigation because it is faster, less expensive and more flexible." *Id.* at 929. In 1958, the Convention was called in an attempt to improve upon previous international agreements and private

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[2] Defendants eschew reliance on the Arbitration Act. *See* Defendants' Memorandum of Law in Further Support ("D. Memo. Further Support") at 12-13.

mechanisms designed to facilitate international arbitration. *Id.* *See*, Quigley, *Accession by the United States to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards*, 70 Yale L.J. 1049, 1051 (1961); McMahon, *Implementation of the United Nations Convention on Foreign Arbitral Awards in the United States*, 2 J.Mar. L.Com. 735, 737 (1971). Although the United States attended and participated in the conference, it did not sign the Convention. "Ten years later, [however,] in 1968, the Senate gave its consent, but accession was delayed until 1970 in order for Congress to enact the necessary implementing legislation." *Bergesen, supra*, 710 F.2d at 929 (citation omitted). As the Supreme Court stated:

> The goal of the Convention, and the principal purpose underlying American adoption and implementation of

> it, was to encourage the recognition and enforcement of commercial arbitration agreements in international contracts and to unify the standards by which agreements to arbitrate are observed and arbitral awards are enforced in the signatory countries.

Scherk v. Alberto-Culver Co., 417 U.S. 506, 520 n.15 (1974) (citations omitted).

In furtherance of this policy, the Convention provides for the recognition or both arbitral agreements and arbitral awards. Article II of the Convention states:

> 1. Each [signatory country] shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration.
>
> . . .
>
> 3. The court of a [signatory country], when seized of an action in a matter in respect of which the parties have made an agreement within the meaning of this article, shall, at the request of one of the parties, refer the parties to arbitration, unless it finds that

> the said agreement is null and void, inoperative or incapable of being performed.

See 9 U.S.C.A. § 201 (1985) (Supp.) (reprinting Convention).

"A court presented with a request to refer a dispute to arbitration pursuant to [the Convention] performs a very limited inquiry." *Ledee v. Ceramiche Ragno*, 684 F.2d 184, 186 (1st Cir. 1982). The Court in *Ledee* reduced the inquiry to four questions:

> (1) Is there an agreement in writing to arbitrate the subject of the dispute? [Citations omitted.]
>
> (2) Does the agreement provide for arbitration in the territory of a signatory of the Convention? [Citations omitted.]
>
> (3) Does the agreement arise out of a legal relationship, whether contractual or not, which is considered as commercial? [Citations omitted.]
>
> (4) Is a party to the agreement not an American citizen, or does the commercial relationship have some reasonable relationship with one or more foreign states? [Citations omitted.]

Id. at 186-87. Therefore, before applying the Convention, the Court must find that all four of these elements are present.

In the instant action, the Superintendent concedes the presence of elements (1), (2) and (4). The written Reinsurance Agreements contain arbitration clauses[3]; the clauses provide for arbitration in the United States and Bermuda, both signatories to the Convention; and defendant is a citizen of Bermuda.[4] Plaintiff, however, contests

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[3] In the arbitration clauses the scope of the duty to arbitrate is defined as follows:

> If any dispute shall arise between the Reinsured and Reinsurer, . . . with reference to the interpretation of this contract or the rights of either party with respect to any transactions under the contract, the dispute shall be referred to [arbitration]. . . .

Gizzi Aff. exhibits B, C, and D, attached thereto.

[4] Under the Convention, a corporation is a United States citizen only if "it is incorporated

(continued...)

whether the third element of the inquiry is present here, as well as the interpretation of the meaning of the that element.

1. *Commercial Relationships and Disputes*

The Convention governs commercial relationships and disputes arising out of those relationships. Therefore, the Superintendent cannot, nor does he, deny that arbitration is appropriate "when two insurers are engaged in a commercial dispute unrelated to any insurance regulatory function." Plaintiff Reply Memorandum ("P. Reply") at 13; *see Ideal Mutual Ins. Co. v. Phoenix Greek Ins.*, No. 83-4687 (S.D.N.Y. July 3, 1984) (Haight, J.); *Hamilton Life Ins. Co. of*

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[4](...continued)
or has its principal place of business in the United States." 9 U.S.C. § 202. Plaintiff does not dispute that Ardra is incorporated and has its principal place of business in Bermuda. *See* Complaint, ¶ 3 ("defendant Ardra is a corporation organized under the laws of and domiciled in Bermuda.")

New York v. Republic National Life Ins. Co., 408 F.2d 606 (2d Cir. 1969); *Ohio Reinsurance Corp. v. British Nat. Ins. Co.*, 587 F. Supp. 710 (S.D.N.Y. 1984). The Superintendent also concedes, as he must, that arbitration is appropriate "where a government entity voluntarily enter[s] into a commercial relationship with a private party. . . ." P. Reply at 13 (citing *Island Territory of Curacao v. Solitron Devices, Inc.*, 356 F. Supp. 1 (S.D.N.Y), *aff'd on other grounds*, 489 F.2d 1313 (2d Cir. 1973), *cert. denied*, 416 U.S. 986 (1974)). The Superintendent, however, submits that the instant action does not fall under either of the aforementioned categories.

The Superintendent points out that Nassau does not have a commercial relationship with Ardra because, as of June 22, 1984, Nassau had no commercial corporate existence, independent of New

York's regulatory scheme for liquidating insolvent insurance companies. *See* N.Y. Ins. Law § 7401 *et. seq.* (McKinney 1985). The Order dissolved Nassau; it states that Nassau's corporate charter is "annulled and forfeited." Order of Liquidation at 3; *see also* N.Y. Ins. Law § 7405 (McKinney 1985). Therefore, the Superintendent is correct that this is not merely a dispute between two private insurers, independent of any regulatory function of the Superintendent. The Superintendent also correctly notes that he was not a party to the Reinsurance Agreements, nor did he bargain to arbitrate with Ardra. Thus, this is also *not* a case where a government entity entered voluntarily into a commercial relationship with a private party.

In addition to demonstrating that the instant dispute does not fall clearly into a category routinely deemed

"commercial" pursuant to the Convention, the Superintendent suggests that "by its own terms, the Convention is not applicable in this case." P. Reply at 19. According to the Superintendent, the "Convention only applies to '*differences* arising out of legal relationships, whether contractual or not, which, are considered as commercial under the national law of the United States.'" *Id.* (quoting the Convention, n. 43) (emphasis added). Thus, the Superintendent argues, "[d]efendants misconstrue the Convention's application by contending that it applies to 'any written agreement *arising out of* a legal relationship which is considered as commercial." P. Reply at 19 (quoting D. Memo. Further Support at 16) (emphasis in defendants' memorandum). This distinction is critical because although the Superintendent concedes that the Reinsurance Agreements initially

arose out of the commercial relationship between Ardra and Nassau, "the *differences* in this action arose out of the relationship between the Superintendent and Ardra." P. Reply at 19 (emphasis in original).

This distinction drawn by the Superintendent is significant if Ardra's relationship with the Superintendent, as the Liquidator of Nassau, is qualitatively different (i.e. regulatory versus commercial) from Ardra's former relationship with Nassau. "The Superintendent contends that he does not stand precisely in Nassau's 'commercial' shoes; that subject to ultimate guidance of the State Supreme Court, [pursuant to Article 74,] the Superintendent's powers as liquidator give him rights which Nassau may not have enjoyed with respect to the reinsurance agreements." P. Reply at 20. Although defendants ostensibly

disagree with the Superintendent, the language of their argument, in effect, supports the Superintendent's position. Defendants state that "*[t]o the extent that [the Superintendent] pursues a right of action on behalf of Nassau . . .* the liquidator is dealing with a dispute which arises out of a commercial relationship." D. Memo. Further Support at 19. It is, however, this precise issue -- to what extent the Superintendent is acting merely as a representative of Nassau -- which the Superintendent argues is the threshold question before the Court.

In addition to suggesting this question as the threshold inquiry of the instant dispute, the Superintendent argues that the question should be answered, in the first instance, by the New York State Supreme Court. The Superintendent points out that the New

York court is more familiar with New York law and therefore is better suited for determining issues of New York law. Moreover, the Court notes that the state courts have a strong interest in furthering the uniform interpretation of the state's law. Furthermore, a finding by the State Supreme Court that the legal relationship between the Superintendent and Ardra is identical to that which existed between Nassau and Ardra, would moot, in this case, defendant's suggested distinction between commercial differences and commercial agreements. Finally, the Superintendent concedes that if the State Supreme Court "agrees with Ardra's view that the Superintendent stands precisely in Nassau's shoes, the Convention will apply and [he] will submit to arbitration." P. Reply at 30. For the above reasons, the Superintendent argues that this Court should abstain

from deciding the instant dispute and instead, remand the case to the New York State Supreme Court.

B. *ABSTENTION*

"As a general rule, the federal courts are under a 'virtually unflagging obligation . . . to exercise the jurisdiction given them.'" *Canady v. Koch*, 608 F. Supp. 1460, 1466 (S.D.N.Y), *aff'd*, 768 F.2d 501 (2d Cir. 1985) (quoting *Colorado River Water Cons. Dist. v. United States*, 424 U.S. 800, 817 (1976)). The Superintendent argues that the instant action "is one of those exceptional cases where the district court should decline to decide a dispute properly before it." *Canady*, *supra*, 608 F. Supp. at 1466. The Superintendent contends that the result he desires is justified under the abstention doctrines of *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943), *Younger v. Harris*, 401 U.S. 37 (1971) and *Colorado River*,

supra, 424 U.S. at 800. The Court will discuss each doctrine separately.

1. *Burford Abstention*

"*Burford* abstention is a consequence of the federalist policy of comity between state and federal sovereignties." *Canady*, *supra*, 608 F. Supp. at 1468. In short, *Burford* abstention allows federal courts "to exercise their discretion to refrain from interfering with state policymaking and enforcement efforts in complex areas which are primarily of state concern and perogative." *Id.*

> [This type of a]bstention is . . . appropriate where there have been presented difficult questions of state law bearing on policy problems of substantial public import whose importance transcends the result in the case then at bar. *Louisiana Power & Light Co. v. City of Thibodaux*, 360 U.S. 25 (1959). . . . *See also Kaiser Steel Corp. v. W.S. Ranch Co.*, 391 U.S. 593 (1968); *Hawks v. Hamill*, 288 U.S. 52 (1933). In some cases, however, the state question itself need not be determinative of state policy. It is enough that exercise of federal review of the question in a case and

> in similar cases would be disruptive of state efforts to establish a coherent policy with respect to a matter of substantial public concern.

Colorado River, *supra*, 424 U.S. at 814.

The above-quoted language indicates that one factor considered by the federal courts in exercising *Burford* abstention is the complexity and uncertainty of state law relevant to the dispute. When the state law issues presented by the action are clear, it is often inappropriate for the federal courts to abstain. *See, e.g., Bd. of Educ. of Valley View v. Bosworth*, 713 F.2d 1316, 1320 (7th Cir. 1983); *Naylor v. Case and McGrath, Inc.*, 585 F.2d 557, 565 (2d Cir. 1978) (abstention is inappropriate where state law is clear because the risk of disrupting state law is negligible). However, "unclear state law . . . is a compelling factor in favor of abstention . . . ." *Canady*, *supra*, 608 F. Supp. at

1468 (citations omitted). Nevertheless, unsettled state law is insufficient, in and of itself, to mandate abstention.

In addition to evaluations of the complexity and uncertainty of the relevant state law, the federal courts should also assess the effect their decisions could have on state programs. "If the federal court's ruling could have 'broad impact on state policy,' *Smith v. Metropolitan Prop. & Liab. Ins. Co.*, 629 F.2d 757, 760 (2d Cir. 1980), then abstention may be proper." *Canady, supra*, 608 F. Supp. at 1468. More specifically, "where a ruling would have wide-ranging effect on what are essentially state and local affairs, federal judiciary intervention would be 'inimical to harmonious federalism.'" *Id.* at 1469 (citations omitted).

A third factor, related, to the two mentioned previously, is the significance

of the state's interest in the subject matter underlying the litigation. In matters where the state has a particularly strong interest -- often matters in which a federal court decision would have broad impact on state policies -- cases brought in the federal courts are more likely to detract, than add, to state attempts to deal rationally with the problem. *Thibodaux*, *supra*, 360 U.S. at 29 ("special nature of eminent domain justifies . . . [abstention]").

The final consideration relevant to the application of the *Burford* doctrine of abstention is the way in which the state is handling the subject matter underlying the litigation. "Existence of a comprehensive system of state administrative decisionmaking with specified channels of judicial review is important to a federal court in deciding to abstain . . . . A specialized review apparatus

assures adequate protection of the parties' rights and attention to the matter by an expert tribunal." *Canady*, *supra*, 608 F. Supp. at 1469 (citing *Burford*, *supra*, 319 U.S. at 333). In short, the existence of a state regulatory scheme supports the exercise by the federal court of *Burford* abstention.

The aforementioned factors highlight the *Burford* doctrine's focus on promoting federal-state relations. These considerations emphasize the nation's interest in allowing states and localities to develop and enforce their own policies, especially in areas traditionally relegated to the province of the states.

With respect to the first factor, the Court notes that the construction of the language of the Convention is initially a question of federal law.

However, this does not bar *Burford* abstention. As the Second Circuit noted:

> In *Burford* itself, violations of federal law were alleged. The claims there amounted to an attack on the reasonableness of the state administrative action. Thus federal review, while involving decisions of a federal question, would have entailed a *reconsideration of the state administrative decision*, carrying with it the potential for creating inequities in the *administration of the state scheme*. *Burford* thus suggests that proper respect for the expertise of state officials and the expeditious and evenhanded administration of state programs counsels restraint on the part of the federal courts.

Levy v. Lewis 635 F.2d 960, 964 (2d Cir. 1980) (emphasis added).

A similar argument may be made in this case. While defendants' request for arbitration involves questions of federal law -- whether the arbitration provisions contained in the Reinsurance Agreements are "commercial" and whether, to the extent that the Superintendent pursues rights of Nassau under the Reinsurance

Agreements, the dispute between the Superintendent and Ardra is "commercial" -- defendants' claim is inextricably intertwined with complex and unsettled issues of state law. For example, to what degree is the superintendent -- saddled with the duty and responsibility of protecting the interests of policyholders, stockholders, and other general creditors -- limited by the contractual rights and obligations negotiated by Nassau in the Reinsurance Agreements. These federal questions, in part dependent upon state questions, are best "left in the first instance to the [state court] with review available . . . ultimately in the United States Supreme Court." *Levy*, *supra*, 635 F.2d at 964.[5]

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[5] Moreover, with respect to the ultimate question of determining whether the McCarran-Ferguson Act, conjoined with Article 74's bestowal of exclusive jurisdiction on the State Supreme Court over insurance liquidation proceeding, takes precedence over the Convention, (continued...)

The second factor federal courts should consider in determining whether they should abstain under *Burford* is whether their ruling could have a broad impact on state policy. The Second Circuit has recognized the importance of liquidation proceedings in the New York state insurance industry. "Liquidation proceedings involve the adjustment of thousands of claims against the insurer by policyholders and those who claim under them, as well as claims by present employees, past employees, and general creditors. Moreover, the claims must be satisfied by marshalling the existing

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[5](...continued)
in the context of international reinsurance agreements, the state court "stands in as good if not a better position than the federal courts to make an initial determination of [the scope of that jurisdiction and the depth of the state's interest.]" *Levy, supra*, 635 F.2d at 964. In fact, defendants expressly decline to argue that the New York state courts would reach a different result than this Court regarding whether the Convention requires arbitration of this dispute. D. Memo. Further Support at 37 n.10.

assets of the insolvent company and by reinsuring existing policies using a state fund established for this purpose." *Id.* at 963.

Defendants argue that this case will not impact on New York's policy concerning the liquidation of insolvent insurers. Defendants contend first that the instant "contract dispute" is not part of New York's regulatory scheme. Furthermore, defendants claim that "this is not a case in which the court is being asked to interpret regulations that could have '"extensive repercussions throughout the insurance industry of the state."'" D. Memo. Further Support at 33 (quoting *Smith, supra*, 629 F.2d at 761) (in turn quoting *Roy v. Centennial Ins. Co.*, 171 Conn. 463, 473, 370 A.2d 1011, 1017 (1976)). Moreover, defendants assert that "this action does not involve the distribution of assets to policyholders

or claimants." D. Memo. Further Support at 33. Defendants' insist that this matter is merely a contract dispute and its referral to an arbitrator "will not interfere in the orderly liquidation of Nassau." *Id.* at 34. Finally, defendants assert blithely that "[r]egardless of the arbitration outcome, claimants under Nassau policies will be paid from the New York State guaranty funds." *Id.* (citing N.Y. Ins. Law, §§ 7405 and 7601(e) (McKinney's 1985)).

In essence, defendants are arguing that New York's entire statutory scheme designed to regulate the liquidation of insolvent insurers has no bearing on the rights of Ardra. Defendants also appear to claim that policyholders or claimants of Nassau have no interest in the

resolution of the dispute between the Superintendent and Ardra. These arguments highlight, rather than alleviate the serious public policy issues involved in these liquidation proceedings.

The Superintendent, under the direction of the State Supreme Court, is authorized to administer liquidation proceedings and the New York Property/Casualty Security Fund (the "Fund"). N.Y. Ins. Law §§ 7405 and 7601(e) (McKinney 1985). In order to comply with these statutory provisions, the Superintendent assumed the responsibility for marshalling and disposing of Nassau's assets to pay creditors, including policyholders. Reinsurance proceeds payable pursuant to the Reinsurance Agreements are assets of Nassau's estate. *See Schenck, supra*, 441 F. Supp. at 723-27; *see also Skandia*

America Reinsurance Corp. v. Barnes, 458 F. Supp. 13, 16 (D. Colo. 1978). In fact, this Court has perceived that "[r]einsurance takes on added significance when the insurer becomes insolvent." *Schenck, supra*, 441 F. Supp. at 724.

Reinsurance proceeds are payable to the Superintendent, for the benefit of all creditors of Nassau's or any other insolvent insurer's estate. The Fund, which pays only policyholders, may maintain a claim against the insolvent insurer and becomes a general creditor thereof. *Id.* at 726. Policyholders, however, have no direct right of action against reinsurers. The Fund, therefore, is not permitted to recover reinsurance proceeds from the insolvent company's reinsurers. Only the Superintendent, as the insurer's Liquidator, can recover from the reinsurer. The Court also notes

that in the instant case the Reinsurance Agreements provide for payments by Ardra to the Liquidator in the event of Nassau's insolvency.[6]

The Fund is supported by statutorily mandated contributions from solvent insurers licensed to do business in New

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[6] Thus, the Reinsurance Agreements appear to contemplate the transformation of the relationship from one of a commercial nature to one of a regulatory nature. The Reinsurance Agreements contain provisions requiring Ardra to pay reinsurance proceeds to the Liquidatior of Nassau if Nassau became insolvent. The provisions are modeled upon § 1308 of N.Y. Ins. Law (formerly § 315). The provisions refer expressly to § 315. Thus, it appears that the parties to the Reinsurance Agreements anticipated, under certain circumstances, the application of New York law to their relationship. Furthermore, pursuant to the laws of New York, when parties make a contract, it is reasonable to infer that they were aware of relevant law, and those laws "must be deemed to have permeated the agreement and constituted elements of the oblgiation." *People v. Globe Mutual Life Insurance Co.*, 91 N.Y. 174, 1979 (1883). This axiom of contract construction has been applied to New York's law of reinsurance and insurer insolvency. *Schenck supra*, 441 F. Supp. at 724; *Matter of Knickerbocker*, 4 N.Y.2d 245, 251, 173 N.Y.S.2d 602, 607, 149 N.E.2d 885, 889 (1958). Therefore, Ardra must be deemed to have had knowledge, at the time it entered into the contract with Nassau, regarding the exclusive jurisdiction of the State Supreme Court with respect to the liquidation of Nassau, and the probable implications of this jurisdiction for the enforceability of each Reinsurance Agreement's arbitration provisions.

York. Therefore, defendants' argument that the mere existence of the Fund alleviates any concern New York should have regarding the instant dispute is completely unfounded. In fact, it is of great public concern that insurers, presently in sound financial condition, not be further burdened with assuming addition liabilities unless absolutely necessary. In other words, the Fund, like many others, is not self-sustaining; it is crucial, therefore, to creditors of the insolvent insurer, as well as to policyholders, stockholders, and creditors of presently solvent insurers -- forced to contribute to the fund -- that the deficit of the insolvent insurer be reduced as much as possible.

In addition to the particular concerns discussed above, the Second Circuit noted that the possibility of the liquidation process being reviewed by two

authorities further supports the exercise of *Burford* abstention in the context of the insurance industry in New York. Relying on the experience of the federal courts in bankruptcy matters, the Circuit Court acknowledged, within the backdrop of insolvent insurance companies, the "importance of consolidating all of the assets of an insolvent company and gathering all those who have claims against those assets *in a single forum*." *Levy*, *supra*, 635 F.2d at 964 (emphasis added).

> Experience has demonstrated that, in order to secure an economical, efficient, and orderly liquidation and distribution of the assets of an insolvent corporation for the benefit of all creditors and stockholders, it is essential that the title, custody, and control of the assets be entrusted to a single management under the *supervision of one court*. Hence other courts, except when called upon by the court of primary jurisdiction for assistance, are excluded from participation. This should be *particularly true as to proceedings for the liquidation of insolvent insurance*

> *companies . . . .*" *Motlow v. Southern Holding & Securities Corp.*, 95 F.2d 721, 725-26 (8th Cir.), *cert. denied*, 305 U.S. 609 (1938) (emphasis added).

The Second Circuit, in applying the *Burford* principles to disputes involving New York's insurance industry, also found it "highly significant that the state scheme has been adopted pursuant to congressional authorization." *Levy*, *supra* 635 F.2d at 963. In particular the Levy Court noted that:

> In the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015, Congress mandated that regulation of the insurance industry be left to the individual states. Thus the administrative and judicial scheme erected by New York to regulate insurance companies, including that part enabling the institution and implementation of liquidation proceedings, operates pursuant to an *express federal policy of noninterference in insurance matters*.

Id. (emphasis added). Therefore, the Circuit Court concluded that it is proper that the "[f]ederal courts have . . . been slow to interrupt such schemes

unless necessary, particulary when federal court action would impinge upon the area in which Congress has recognized the overriding interest of the States." *Id.* at 963-64.

Finally, as discussed previously, federal courts must also consider "*Burford's* concern with noninterruption of state administrative programs . . . ." *Id.* at 963. As the Second Circuit has explained, "the federal courts have abstained in numerous areas where . . . state policies were carried out in a statutorily established regulatory program by state officials." *Id.* (citations omitted). "In this case, New York State has a complex administrative and judicial system for regulating and liquidating domestic insurance companies. [Citation omitted] The Superintendent . . . is an experienced state official who has been involved both in

rehabilitating and liquidating [domestic insurance companies]." *Id.* Moreover, "[l]iquidation in particular is an area in which the Superintendent's expertise is critical." *Id.*

The federal courts applying the *Burford* doctrine must also be concerned with how effectively the state's "specialized review apparatus assures adequate protection of the parties' rights . . .", *Canady, supra*, 608 F. Supp. at 1469, as well as the apparatus' expertise. Defendants cannot argue that proceedings before the State Supreme Court do not adequately serve to protect their rights. Defendants can raise the arbitration question before the State Supreme Court. In fact, as defendants, themselves, point out, the New York courts are familiar with the law governing the Convention and the importance of international arbitration

agreements. D. Memo. Further Support at 37 n.10. It is also clear that remanding this case does not foreclose final review of the decision by a federal court, but merely affords the state court the opportunity to clarify an uncertain area of state law, while at the same time enabling this Court to avoid deciding a novel question of federal law prematurely.

For the aforementioned reasons, the teaching of *Burford* support application here of the policies behind abstention.

2. *Younger Abstention*

Plaintiff also argues that the *Younger* abstention doctrine is appropriate here. "*Younger* held that a federal court should not entertain suits challenging state action when the state has already initiated proceedings in the state courts in which the plaintiff is able to raise federal claims." *Levy*,

supra, 635 F.2d at 964. Although *Younger* was a criminal matter, the Supreme Court has stated that the reasoning underlying *Younger* may warrant abstention in civil matters as well. *See Moore v. Sims*, 442 U.S. 415 (1979). In *Moore*, the Court noted that *Younger* principles of comity express:

> . . . a strong policy against federal intervention in state judicial processes in the absence of great and immediate irreparable injury to the federal plaintiff. *Samuels v. Mackell*, 401 U.S. 66, 69 (1971). That policy was first articulated with reference to state criminal proceedings, but as we recognized in *Huffman v. Pursue, Ltd.*, 420 U.S. 592 (1975), the basic concern -- that threat to our federal system posed by displacement of state courts by those of the National Government -- is also fully applicable to civil proceedings in which important state interests are involved.

422 U.S. at 423.

The Supreme Court has not yet applied *Younger* abstention to state insurance liquidation proceedings.

"[W]hile these proceedings are perhaps more remote from the criminal process than other proceedings in which *Younger* has been applied, [*see Juidice v. Vail*, 430 U.S. 327 (1977) (enforcement of contempt proceedings); and *Trainor v. Hernandez*, 431 U.S. 434 (1977) (fiscal integrity of public assistance programs),] *Younger's* concerns with comity and with a state's enforcement of important state interests in its own courts seem equally applicable." *Levy*, *supra*, 635 F.2d at 965.

Defendants contend that this is not a case from which the Court should abstain on the basis of *Younger* and its progeny. In support of their argument, defendants mischaracterize, once again, this action as a "garden variety contract action . . . through which plaintiff seeks a definite sum of money." D. Memo. Further Support at 36. Defendants ignore

the fact that "[h]ere, the state is a party to proceedings in its own courts [prior to defendants removal], seeking to carry out regulatory duties left to it by Congress." *Levy*, *supra*, 635 F.2d at 965. There is more at stake here -- the interests of policyholders and other creditors of Nassau; the interests of currently solvent insurers and parties interested in their financial well-being; and the interest of the State in maintaining an orderly system for regulating the insurance industry -- than a simple contract dispute between an insolvent insure and its reinsurer. Moreover, as was discussed at greater length during this Court's analysis of the *Burford* doctrine, defendants can raise their federal claims in the State Supreme Court, as well as in this Court. Thus, the Court finds that the principles of *Younger* also support abstention.

3. *Colorado River Abstention*

Plaintiff also argues that another category of abstention, that is recognized in *Colorado River*, *supra*, 424 U.S. at 800, is applicable here. "In *Colorado River*, the Supreme Court synthesized prior authority and announced a narrow exception to the duty of federal courts to exercise the jurisdiction granted to them." *Canady*, *supra*, 608 F. Supp. at 1473. The Court found that even in the absence of the other abstention doctrines, "federal courts ought to refuse to decide cases when considerations of '[w]ise judicial administration giving regard to conservation of judicial resources and comprehensive disposition of litigation,' . . . require abstention." *Levy*, *supra*, 635 F.2d at 965 (quoting *Colorado River*, *supra*, 424 U.S. at 817) (citation omitted). The principle underlying

Colorado River abstention is a prudential concern, "a second court with concurrent jurisdiction will exercise its discretion to defer to another court for the sake of comprehensive disposition of rights in a particular piece of property or in a fund." *Levy, supra*, 635 F.2d at 966.

The factors to be weighed by the federal courts in applying the *Colorado River* or "exceptional circumstances test" are:

> 1) The inconvenience of the federal forum;
>
> 2) Order in which jurisdiction was obtained by the forums;
>
> 3) Desirability of avoiding piecemeal litigation;
>
> 4) Presence or absence of substantial progress in the federal litigation;
>
> 5) Whether state or federal law provides the rule of decision on the merits; and
>
> 6) Adequacy of the state proceeding to protect the federal plaintiff's rights.

Moses H. Cone Memorial Hospital v. Mercury Constr. Corp., 460 U.S. 1, 15-16 (1983) (citing, in part, *Colorado River, supra*, 424 U.S. at 818-19). These factors must not be applied mechanically, but instead should be balanced carefully, "with the balance heavily weighted in favor of the exercise of jurisdiction." *Id.* at 16.

The Court notes that jurisdiction over this dispute was first obtained by the State Supreme Court when the Superintendent commenced this action on April 29, 1985. Defendants did not seek arbitration until after the action was filed. Moreover, defendants waited almost four months before removing this action to this Court. There has not been substantial progress in the federal litigation. On the other hand, the Superintendent does not contend that the federal forum is inconvenient. In any

event, the other factors referred to by the Supreme Court in *Moses H. Cone* are more telling in this case.

Even prior to *Colorado River*, federal courts, in an effort to avoid piecemeal litigation, have deferred in cases involving disposition of assets of insolvent companies, especially in the context of the insurance industry. *See Levy, supra*, 635 F.2d at 966. The Circuit Court cited the "strong prudential reasons for requiring that all claims brought against a single fund or pool of assets of an insolvent company should be heard in a single forum." *Id.* (citation omitted). Of course, this case does not directly involve claims against the Fund or against the assets of Nassau, as managed by the Superintendent; however, for the reasons discussed earlier, these same policy concerns are implicated here.

In addition to the need for unified proceedings for determining the disposition of Nassau's assets, the federal policy -- embodied in the McCarran-Ferguson Act -- of delegating the regulation of insurance companies to the states, augurs in favor of the exercise of abstention under the *Colorado River* doctrine. In addition, as explained during the analysis of the *Burford* doctrine, defendants cannot argue that proceedings before the State Supreme Court are not adequate to protect their rights regarding this dispute. Moreover, in light of the Superintendent's position that an adverse holding by the State Supreme Court with respect to his legal status under the contract would moot his objections to defendants' arbitration demand, the Court believes that abstention by this Court serves the

prudential interests embodied by *Colorado River* abstention.

Defendants argue that *Colorado River* abstention is inappropriate in this case because it is federal law which provides the rule of decision in this case. However, as discussed previously, to determine whether or not the Convention applies to the instant dispute, the Court must first determine the status of the Superintendent. The determination of the powers of the Superintendent is a question of state law. The Supreme Court of the State of New York is in the best position to interpret New York law. Thus, this factor also argues in favor of abstention.

CONCLUSION

For the aforementioned reasons, the Court hereby grants the Superintendent's motion seeking remand of this action to the New York State Supreme Court. The

Court notes that its decision does not suggest anything concerning the merits of the Superintendent's claim for reinsurance proceeds under the Reinsurance Agreements. Nor should this decision be read to imply anything regarding the novel question of whether the McCarran-Ferguson Act, conjoined with New York's regulatory system for liquidating insolvent insurers, takes precedence over the Convention. This decision is limited to this Court deferring to the State Supreme Court to interpret an issue of state law, so the threshold question in this action, whether the Convention applies to this dispute can be answered in a more logical and efficient manner.

SO ORDERED.

Dated: New York, New York
April 16, 1987

CONSTITUTION OF THE UNITED STATES OF AMERICA

ARTICLE I

* * *

Section. 8. The Congress shall have Power

. . .

To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes;

* * *

ARTICLE VI

* * *

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or

Laws of any State to the Contrary notwithstanding.

Convention on the Recognition and Enforcement of Foreign Arbitral Awards

Article I

1. This Convention shall apply to the recognition and enforcement of arbitral awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought, and arising out of differences between persons, whether physical or legal. It shall also apply to arbitral awards not considered as domestic awards in the State where their recognition and enforcement are sought.

2. The term "arbitral awards" shall include not only awards made by arbitrators appointed for each case but also those made by permanent arbitral bodies to which the parties have submitted.

3. When signing, ratifying or acceding to this Convention, or notifying

extension under article X hereof, any State may on the basis of reciprocity declare that it will apply the Convention to the recognition and enforcement of awards made only in the territory of another Contracting State. It may also declare that it will apply the Convention only to differences arising out of legal relationships, whether contractual or not, which are considered as commercial under the national law of the State making such declaration.

Article II

1. Each Contracting State shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration.

2. The term "agreement in writing" shall include an arbitral clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams.

3. The court of a Contracting State, when seized of an action in a matter in respect of which the parties have made an agreement within the meaning of this article, shall, at the request of one of the parties, refer the parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed.

Article III

Each Contracting State shall recognize arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the award is relied upon, under the conditions laid down in the following

articles. There shall not be imposed substantially more onerous conditions or higher fees or charges on the recognition or enforcement of arbitral awards to which this Convention applies than are imposed on the recognition or enforcement of domestic arbitral awards.

Article IV

1. To obtain the recognition and enforcement mentioned in the preceding article, the party applying for recognition and enforcement shall, at the time of the application, supply:

(a) The duly authenticated original award or a duly certified copy thereof;

(b) The original agreement referred to in article II or a duly certified copy thereof.

2. If the said award or agreement is not made in an official language of the country in which the award is relied upon, the party applying for recognition

and enforcement of the award shall produce a translation of these documents into such language. The translation shall be certified by an official or sworn translator or by a diplomatic or consular agent.

Article V

1. Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that:

(a) The parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made; or

(b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or

(c) The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contain decisions on matters submitted to arbitration may be recognized and enforced; or

(d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement,

was not in accordance with the law of the country where the arbitration took place; or

(e) The award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.

2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:

(a) The subject matter of the difference is not capable of settlement by arbitration under the law of that country; or

(b) The recognition or enforcement of the award would be contrary to the public policy of that country.

Article VI

If an application for the setting aside or suspension of the award has been made to a competent authority referred to in article V(1)(e), the authority before which the award is sought to be relied upon may, if it considers it proper, adjourn the decision on the enforcement of the award and may also, on the application of the party claiming enforcement of the award, order the other party to give suitable security.

Article VII

1. The provisions of the present Convention shall not affect the validity of multilateral or bilateral agreements concerning the recognition and enforcement of arbitral awards entered into by the Contracting States nor deprive any interested party of any right he may have to avail himself of an arbitral award in the manner and to the extent allowed by the law or the treaties of the county

[sic] where such award is sought to be relied upon.

2. The Geneva Protocol on Arbitration Clauses of 1923 and the Geneva Convention on the Execution of Foreign Arbitral Awards of 1927 [27 LNTS 157; 92 LNTS 301] shall cease to have effect between Contracting States on their becoming bound and to the extent that they become bound, by this Convention.

Article VIII

1. This Convention shall be open until 31 December 1958 for signature on behalf of any Member of the United Nations and also on behalf of any other State which is or hereafter becomes a member of any specialized agency of the United Nations, or which is or hereafter becomes a party to the Statute of the International Court of Justice [T.S. 993; 59 Stat. 1055], or any other State to

which an invitation has been addressed by the General Assembly of the United Nations.

2. This Convention shall be ratified and the instrument of ratification shall be deposited with the Secretary-General of the United Nations.

Article IX

1. This Convention shall be open for accession to all States referred to in article VIII.

2. Accession shall be effected by the deposit of an instrument of accession with the Secretary-General of the United Nations.

Article X

1. Any State may, at the time of signature, ratification or accession, declare that this Convention shall extend to all or any of the territories for the international relations of which it is responsible. Such a declaration shall

take effect when the Convention enters into force for the State concerned.

2. At any time thereafter any such extension shall be made by notification addressed to the Secretary-General of the United Nations and shall take effect as from the ninetieth day after the day of receipt by the Secretary-General of the United Nations of this notification, or as from the date of entry into force of the Convention for the State concerned, whichever is the later.

3. With respect to those territories to which this Convention is not extended at the time of signature, ratification or accession, each State concerned shall consider the possibility of taking the necessary steps in order to extend the application of this Convention to such territories subject, where necessary for constitutional reason, to

the consent of the Governments of such territories.

Article XI

In the case of a federal or non-unitary State, the following provisions shall apply:

(a) With respect to those articles of this Convention that come within the legislative jurisdiction of the federal authority, the obligations of the Federal Government shall to this extent be the same as those of Contracting States which are not federal States;

(b) With respect to those articles of this Convention that come within the legislative jurisdiction of constituent states or provinces which are not, under the constitutional system of the federation, bound to take legislative action, the federal Government shall bring such articles with a favourable recommendation to the notice of the

appropriate authorities of constituent states or provinces at the earliest possible moment;

(c) A federal State Party to the Convention shall, at the request of any other Contracting State transmitted through the Secretary-General of the United Nations, supply a statement of the law and practice of the federation and its constituent units in regard to any particular provision of this Convention, showing the extent to which effect has been given to that provision by legislative or other action.

Article XII

1. This Convention shall come into force on the ninetieth day following the date of deposit of the third instrument of ratification or accession.

2. For each State ratifying or acceding to this Convention after the deposit of the third instrument of

ratification or accession, this Convention shall enter into force on the ninetieth day after deposit by such State of its instrument of ratification or accession.

Article XIII

1. Any Contracting State may denounce this Convention by a written notification to the Secretary-General of the United Nations. Denunciation shall take effect one year after the date of receipt of the notification by the Secretary-General.

2. Any State which has made a declaration or notification under article X may, at any time thereafter, by notification to the Secretary-General of the United Nations, declare that this Convention shall cease to extend to the territory concerned one year after the date of the receipt of the notification by the Secretary-General.

3. This Convention shall continue to be applicable to arbitral awards in respect of which recognition or enforcement proceedings have been instituted before the denunciation takes effect.

Article XIV

A Contracting State shall not be entitled to avail itself of the present Convention against other Contracting States except to the extent that it is itself bound to apply the Convention.

Article XV

The Secretary-General of the United Nations shall notify the States contemplated in article VIII of the following:

(a) Signatures and ratifications in accordance with article VIII;

(b) Accessions in accordance with article IX;

(c) Declarations and notifications under articles I, X and XI;

(d) The date upon which this Convention enters into force in accordance with article XII;

(e) Denunciations and notifications in accordance with article XIII.

Article XVI

1. This Convention, of which the Chinese, English, French, Russian and Spanish texts shall be equally authentic, shall be deposited in the archives of the United Nations.

2. The Secretary-General of the United Nations shall transmit a certified copy of this Convention to the States contemplated in article VIII.

Done at New York June 10, 1958: entered into force for the United States December 29, 1970, subject to declarations.

FEDERAL ARBITRATION ACT, 9 U.S.C. §§ 201-208

* * *

CHAPTER 2 - CONVENTION ON THE RECOGNITION AND ENFORCEMENT OF FOREIGN ARBITRAL AWARDS

§ 201. Enforcement of Convention

The Convention on the Recognition and Enforcement of Foreign Arbitral Awards of June 10, 1958, shall be enforced in United States courts in accordance with this chapter.

§ 202. Agreement or award falling under the Convention

An arbitration agreement or arbitral award arising out of a legal relationship, whether contractual or not, which is considered as commercial, including a transaction, contract, or agreement described in section 2 of this title, falls under the Convention. An agreement or award arising out of such a relationship which is entirely between citizens

of the United States shall be deemed not to fall under the Convention unless that relationship involves property located abroad, envisages performance of enforcement abroad, or has some other reasonable relation with one or more foreign states. For the purpose of this section a corporation is a citizen of the United States if it is incorporated or has its principal place of business in the United States.

§ 203. Jurisdiction; amount in controversy

An action or proceeding falling under the Convention shall be deemed to arise under the laws and treaties of the United States. The district courts of the United States (including the courts enumerated in section 460 of title 28) shall have original jurisdiction over

such an action or proceeding, regardless of the amount in controversy.

§ 204. Venue

An action or proceeding over which the district courts have jurisdiction pursuant to section 203 of this title may be brought in any such court in which save for the arbitration agreement an action or proceeding with respect to the controversy between the parties could be brought, or in such court for the district and division which embraces the place designated in the agreement as the place of arbitration if such place is within the United States.

§ 205. Removal of cases from State courts

Where the subject matter of an action or proceeding pending in a State court relates to an arbitration agreement or award falling under the Convention,

the defendant or the defendants may, at any time before the trial thereof, remove such action or proceeding to the district court of the United States for the district and division embracing the place where the action or proceeding is pending. The procedure for removal of causes otherwise provided by law shall apply, except that the ground from removal provided in this section need not appear on the face of the complaint but may be shown in the petition for removal. For the purposes of Chapter 1 of this title any action or proceeding removed under this section shall be deemed to have been brought n the district court to which it is removed.

§ 206. Order to compel arbitration; appointment of arbitrators

A court having jurisdiction under this chapter may direct that arbitration

be held in accordance with the agreement at any place therein provided for, whether that place is within or without the United States. Such court may also appoint arbitrators in accordance with the provisions of the agreement.

§ 207. Award of arbitrators; confirmation; jurisdiction; proceeding

Within three years after an arbitral award falling under the Convention is made, any party to the arbitration may apply to any court having jurisdiction under this chapter for an order confirming the award as against any other party to the arbitration. The court shall confirm the award unless it finds one of the grounds for refusal or deferral or recognition or enforcement of the award specified in the said Convention.

§ 208. Chapter 1; residual application

Chapter 1 applies to actions and proceedings brought under this chapter to the extent that that chapter is not in conflict with this chapter or the Convention as ratified by the United States.

McCARRAN-FERGUSON ACT, 15 U.S.C. § 1012

* * *

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, . . . unless such Act specifically relates to the business of insurance . . . .

* * *

Supreme Court, U.S.
FILED
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No. 90-1567

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

ARDRA INSURANCE COMPANY LTD., et al.,

Petitioners,

vs.

SALVATORE R. CURIALE, SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK, AS LIQUIDATOR OF NASSAU INSURANCE COMPANY, IN LIQUIDATION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI
TO THE NEW YORK STATE COURT OF APPEALS

RESPONDENT'S BRIEF IN OPPOSITION

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COUNTERSTATEMENT OF QUESTIONS PRESENTED

1. Whether the statutory Liquidator of an insolvent insurer is bound by the insurer's pre-liquidation arbitral agreement with a Bermuda affiliate?

2. Whether the statutory liquidation of an insolvent insurer, centralizing its affairs in a State Liquidation Court, renders its pre-liquidation arbitral agreements "null and void, inoperative or incapable of being performed" within the meaning of Article II.3 of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards?

3. Whether the McCarran-Ferguson Act bars application of the Convention to compel the statutory Liquidator of an insolvent insurer to arbitrate claims for reinsurance proceeds due from an alien reinsurer?

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No. 90-1567

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PETITION FOR A WRIT OF CERTIORARI
TO THE NEW YORK STATE COURT OF APPEALS

RESPONDENT'S BRIEF IN OPPOSITION

Respondent Salvatore R. Curiale, Superintendent of Insurance of the State of New York, as Liquidator of Nassau Insurance Company (the "Liquidator") respectfully submits this Brief in Opposition to the petition for writ of certiorari to the New York Court of Appeals.

COUNTERSTATEMENT OF THE CASE

Nassau Insurance Company ("Nassau") was a stock casualty insurer, licensed by the New York Department of Insurance and ultimately owned by petitioners Richard A. DiLoreto and Jeanne S. DiLoreto (the "DiLoretos"), both of whom are New York residents (PA:3).[1] Nassau conducted its business in New York, with Richard DiLoreto as its president (*id.*). In 1976, the DiLoretos established Ardra, as a Bermuda corporation, to reinsure risks originally underwritten by Nassau. Jeanne S. DiLoreto served as president of Ardra (*id.*). Nassau paid Ardra over $10 million in reinsurance premiums (PA:4).

On June 22, 1984, Nassau was placed in liquidation by order of New York State Supreme Court Justice Leonard N. Cohen (the "Liquidation Order") (RA:1). The Liquidation Order dissolved the insolvent Nassau, terminated all its subsisting contracts and other obligations (with "all liability thereunder [to] cease and be fixed" as of the date of the order), appointed the Superintendent of Insurance of the State of New York as Liquidator, vested the Liquidator with "title to all of the property, contracts and rights of action" of Nassau, and directed "that all persons indebted to NASSAU INSURANCE COMPANY render accounts of their indebtedness and pay any sums due to the Superintendent of Insurance as Liquidator" (RA:3-4, 7).

After the liquidation commenced, Ardra began to balk at paying losses under the reinsurance contracts, challenging the Liquidator's handling of claims on which Ardra had exposure. On February 13, 1985, approximately 20 actions involving claims against Nassau were scheduled for settlement conferences before Justice Stanley Parness in Supreme Court, New York County (CA:100). Richard DiLoreto, who by then had become president of Ardra, appeared on the reinsurer's behalf along with an attorney (*id.*). On the application of the Liquidator, Justice Parness excluded them from the conferences (*id.*).

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[1] References to PA:__ are to the Petitioners' Appendix; references to RA:__ are to the Respondent's Appendix; references to CA:__ are to the appendix in the New York Court of Appeals.

Within a week, Ardra disclaimed its liabilities under the reinsurance contracts on grounds that the Liquidator had breached the contracts' "association in the defense" clause (CA:100-102). Thereafter, the Liquidator commenced this action for the reinsurance proceeds due from Ardra (CA:218). The Liquidator also seeks recovery from the DiLoretos as *alter egos* of Ardra and for breach of their fiduciary duties to Nassau (CA:229-236).

In the proceedings below, the petitioners maintained that the arbitration clauses in the contracts between the two DiLoreto companies were enforceable against the respondent under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 21 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.S. 38, as implemented at 9 U.S.C. §§ 201-208 (the "Convention"). After removal from the State Court to the United States District Court for the Southern District of New York, that court abstained in deference to New York's comprehensive regulatory scheme for insurer insolvencies (PA:85-135) and a panel of the United States Court of Appeals for the Second Circuit unanimously affirmed (PA:57-84). The Liquidation Court ruled that the arbitration clauses were not enforceable against the respondent (PA:41-56), a unanimous panel of the Appellate Division, First Department affirmed (PA:22-35), and that decision was, in turn, affirmed by a unanimous New York Court of Appeals (PA:1-21).

The Court of Appeals found that the reinsurance agreements "fall within the general scope of the Convention" (PA:12), but that, because Article II of the Convention does not require arbitration where the controversy does not "concern a subject matter capable of settlement by arbitration" (Art. II.1) or where the arbitral agreement is "null and void, inoperative or incapable of being performed" (Art. II.3), the intervention of New York's statutory scheme for liquidating insolvent insurers precluded arbitration (PA:12-16). The decision of the Court of Appeals is reported at 77 N.Y.2d 225, 566 N.Y.S.2d 75 (1990).

REASONS FOR DENYING THE WRIT

The Court of Appeals' finding that Nassau's arbitral agreements do not bind its Liquidator constitutes independent

and adequate state grounds for decision (Point I). In any event, the Court properly applied the Convention's provision for non-enforcement of arbitral agreements that are "null and void, inoperative or incapable of being performed" (Point II). The Court's reference to the McCarran-Ferguson Act does not create a conflict with decisions of the Fourth and Ninth Circuits (Point III). Finally, compelling statutory liquidators to arbitrate with reinsurers would seriously impair state schemes for the orderly liquidation of insolvent insurers (Point IV).

I.

THE DETERMINATION THAT THE LIQUIDATOR IS NOT BOUND BY NASSAU'S ARBITRAL AGREEMENTS RESTS UPON INDEPENDENT AND ADEQUATE STATE LAW GROUNDS

State law determines who is bound by an arbitral agreement and, in this case, the New York Court of Appeals has authoritatively determined that the Liquidator does not succeed to Nassau's agreements to arbitrate with Ardra. Because the decision below rests on independent and adequate state law grounds, this Court lacks jurisdiction. *Herb v. Pitcairn*, 324 U.S. 117, 125-26 (1945); *Zacchini v. Scripps-Howard Broadcasting Co.*, 443 U.S. 562, 566 (1977); *Michigan v. Long*, 463 U.S. 1032 (1983). *Cf. Kirkpatrick v. Christian Homes of Abilene, Inc.*, 460 U.S. 1074 (1983).

The Court of Appeals concluded that, whatever their vitality during the companies' operating lives,[2] the arbitration clauses do not bind the Liquidator. Article II.3 of the Convention only requires reference to arbitration where the parties to an action "have made an agreement" to submit to arbitration (PA:140). Congress passed the Federal Arbitration Act "to enforce private

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[2] As a practical matter, the arbitration clauses relied upon by petitioners were an illusory feature of the subject reinsurance agreements. As the Court of Appeals recognized, "[t]he DiLoretos were the principals of Ardra and Nassau and both companies were wholly owned by them" (PA:19). So long as the two companies were going concerns, any dispute between them – even if one could conceivably arise – would be resolved by their common owners, not by arbitrators.

agreements *into which parties had entered.*" *Mitsubishi Motors Corporation v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 625 (1985) (emphasis supplied). The Liquidator has entered into no such agreement. Nor is he, as a matter of New York law, so identified with the defunct insurer that he succeeds to its arbitral agreements.[3]

State law determines whether a contract containing an agreement to arbitrate is binding upon a particular party. In a case considered under the Convention, the Eighth Circuit recently looked to state law to determine whether a party was bound by an arbitral agreement: "[i]n addressing the issue of whether a party has entered into an agreement to arbitrate under the Arbitration Act, courts are to apply general state law principles, giving due regard to the federal policy favoring arbitration." *Recold, S.A. De C.V. v. Montfort of Colorado, Inc.*, 893 F.2d 195, 197 (8th Cir. 1990) (following *Volt Information Sciences, Inc. v. Board of Trustees*, 489 U.S. 468 (1989)). Aside from holding that courts should apply "general state-law principles of contract interpretation to an arbitration agreement within the scope of the [Federal Arbitration Act]," 489 U.S. at 1254, *Volt* states that "the FAA does not require parties to arbitrate when they have not agreed to do so" and that "[a]rbitration under the Act is a matter of consent, not coercion." *Id.* at 1255. *See also Valero Refining, Inc. v. M/T Lauberhorn*, 813 F.2d 60, 64 (5th Cir. 1987) ("[o]rdinary contract principles determine who is bound by a written arbitration agreement"); *A/S Custodia v. Lessin International Inc.*, 503 F.2d 318, 320 (2d Cir. 1974) (*per curiam*) (same).[4]

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[3] *Cf. Allegaert v. Perot*, 548 F.2d 432, 435-36 (2d Cir. 1977), declining to compel the trustee of a defunct securities firm to arbitrate a claim against the firm's controlling shareholder: "The trustee's position that he and the bankrupt are different legal entities is certainly correct. . . . [A] bankruptcy trustee is a new entity. . . with [his] own rights, subject to the supervision of the bankruptcy court."

[4] It bears emphasis that the Liquidator is not "assuming" an executory contract of the insolvent insurer and thus obligating himself upon it. *Cf.* Bankruptcy Code, 11 U.S.C. § 365. Aside from dissolving Nassau, the Liquidation Order terminated all of its subsisting contracts and other obligations, providing that "all liability thereunder cease and be fixed" as of the date of the order (RA:4). The Liquidator simply seeks to collect upon defendants' outstanding liabilities to Nassau as fixed in accordance with the Liquidation Order.

The Court of Appeals determined that, "Nassau no longer exists" and respondent "holds office as liquidator solely to protect the interests of policyholders, stockholders, and the public. . ." (PA:15).[5] To effectuate "New York's strong public policy concerns by maintaining the Supreme Court's exclusive jurisdiction over liquidation proceedings," the court ruled that Nassau's private commercial agreements to arbitrate would not be extended to bind its Liquidator and preclude litigation of matters affecting insureds and third-party claimants. (PA:17-18).

The New York Court of Appeals correctly relied upon state law in concluding that the extinguishment of Nassau's corporate existence, the cessation of its business, and the introduction of policyholder interests and the public interest generally, foreclose any duty to arbitrate (PA:14-16). The Liquidator has not, directly or by virtue of his successorship to Nassau's assets, "made an agreement to arbitrate" within Article II.3 and the Court of Appeals' determination is conclusive on that point.

II.

THE COURT OF APPEALS DID NOT ERR IN HOLDING THE ARBITRATION CLAUSES "NULL AND VOID, INOPERATIVE OR INCAPABLE OF BEING PERFORMED" UNDER ARTICLE II.3 OF THE CONVENTION

The Convention states specific exceptions to the enforceability of arbitral agreements. Apart from restricting recognition of arbitral agreements to controversies "concerning a subject matter capable of settlement by arbitration" (Art. II.1), the

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[5] Of these constituencies, the Nassau stockholders' interests are most attenuated by the insolvency, while the policyholder and public interests have, by the same exigency, come to the fore. Yet the petitioners would exalt a phantom commitment of the stockholders – from one of their companies to another of their companies – over the paramount concerns of policyholders and of the public, who never agreed, directly or vicariously, to arbitrate.

Convention authorizes non-enforcement where the arbitral agreement is "null and void, inoperative or incapable of being performed" (Art. II.3).

Quoting from *Mitsubishi*, 473 U.S. at 639 n.21, petitioners contend that only Congress can except a particular subject matter from arbitration under the Convention (Petition at 33). Although the Court of Appeals used the term "subject matter" in finding this dispute non-arbitrable, the term was not used in the same sense as it is employed in the Convention (Art. II.1) or in this Court's decision in *Mitsubishi*. The court did not find that liability under reinsurance agreements is non-arbitrable subject matter. It found that the intervention of New York's liquidation process, and the duties and limitations that that process imposes upon the Liquidator, bar enforcement of the arbitration clauses against the Liquidator (PA:16) ("[t]he Legislature has not granted the Superintendent the authority to arbitrate disputes and under the [liquidation] statute's provisions, the subject matter of the claims against Ardra must be litigated in [the Liquidation] Court"). The court's decision is not an "impermissable nullification of [Art. II.1 of] the Convention" as construed by *Mitsubishi* (Petition at 34); it is a straightforward application of the Article II.3 exceptions.

Relying upon its prior holding in *Knickerbocker Agency, Inc. [Holz]*, 4 N.Y.2d 245, 173 N.Y.S.2d 602, 149 N.E.2d 885 (1958), the court properly held that the intervention of New York's statutory liquidation scheme and the appointment of the Liquidator triggered the Article II.3 exceptions. Petitioners ardently contend that these exceptions to enforceability apply only to "internationally recognized defenses such as duress, mistake, fraud, or waiver" (Petition at 34) (*quoting Rhone Mediterranee Compagnia Francese v. Lauro*, 712 F.2d 50, 53 (3d Cir. 1983); *Ledee v. Ceramiche Ragno*, 684 F.2d 184, 187 (1st Cir. 1982); *I.T.A.D. Assocs. v. Podar Bros.*, 636 F.2d 75, 77 (4th Cir. 1981); *Oriental Commercial & Shipping Co. v. Rosseel, N.V.*, 609 F. Supp. 75, 78 (S.D.N.Y. 1985)). However, they offer no basis for concluding that the insolvency of a contracting party and the appointment of a Liquidator does not impair an arbitral

agreement every bit as much as the circumstances included in that illustrative list.

The advent of insolvency always introduces new interests to the formerly private commercial arrangements of the debtor and commonly requires the centralization of claims by and against the debtor in the insolvency court. This is an internationally recognized fact of business life. For example, a federal Bankruptcy Court may decline to compel a bankruptcy trustee to arbitrate claims arising under the debtor's contracts, at least where the trustee has not "assumed" those contracts pursuant to the Bankruptcy Code, 11 U.S.C. § 365.[6]

Enforcement of a bankrupt's arbitral agreement will be denied where arbitration "would seriously jeopardize the objectives of the [Bankruptcy] Code." *Hays & Co. v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 885 F.2d 1149, 1161 (3rd Cir. 1989). The court or court system responsible for administering the insolvency is best situated to make the judgment that arbitration would so jeopardize the insolvency scheme in a given case. Because insurer insolvencies are excluded from the federal bankruptcy system, 11 U.S.C. § 109[b][2], and administered by a state liquidation court, that court, under the supervision of the state appellate courts, is appropriately vested with responsibility to measure possible jeopardy to the state scheme. Here, where Ardra sets up the Liquidator's own conduct in excluding the reinsurer's representatives from settlement conferences as the basis for withholding reinsurance proceeds and collaterally attacks a judicial determination upholding that exclusion, the state courts' judgment that arbitration would impair New York's liquidation scheme is entitled to stand. The intervening insolvency has made Nassau's arbitral agreements "null and void, inoperative or incapable of being performed."

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[6] Bermuda law is very similar. Where the trustee in bankruptcy does not "adopt" a contract including an arbitration clause, the enforceability of that clause is committed to the Bankruptcy Court's discretion, which is to be exercised "having regard to all the circumstances of the case. . . ." Bermuda Arbitration Act of 1986, § 6.

Granting the primacy of state law is most necessary where a party's capability of performing the arbitral agreement is in question and that party is fulfilling a role ordained by state statute and functioning under the supervision of a state court.[7] New York's highest court has held that "absent express authority to do so, the Superintendent [cannot] engage in arbitration when acting as a liquidator" and that "the legislature has not granted the Superintendent the authority to arbitrate disputes" (PA:16). Compelling arbitration in such circumstances would consign the Liquidator to a legal no man's land — statutorily and judicially precluded from arbitrating and federally barred from a judicial forum.

III.

THE COURT OF APPEALS DID NOT ERR IN CLASSIFYING THIS ASPECT OF NASSAU'S LIQUIDATION AS THE "BUSINESS OF INSURANCE" WITHIN McCARRAN-FERGUSON — IF THAT IS WHAT IT DID

Petitioners address their primary challenge to what the Court of Appeals "necessarily held" concerning the "business of insurance," i.e., that the liquidation of an insolvent insurer, taken as a whole, is the business of insurance within McCarran-Ferguson. However, the court's opinion does not even discuss the point. To contrive a cert-worthy question, the petitioners would wrest from the opinion below the implicit holding that the liquidation of an insolvent insurer *is* the business of insurance (when, at best, the court implied that a liquidator's collection of reinsurance proceeds is the business of insurance). Then, the petitioners would set that putative holding in opposition to two federal circuit decisions which are represented to hold that the liquidation of insolvent insurers is *not* the business of

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[7] These circumstances also distinguish the case from *Mitsubishi* where the Court upheld enforcement of an arbitral agreement against a private antitrust plaintiff: "the antitrust cause of action remains at all times under the control of the individual litigant; no citizen is under an obligation to bring an antitrust suit and the private antitrust plaintiff needs no executive or judicial approval before settling one." 473 U.S. at 636 (citations omitted).

insurance (when, in fact, those cases hold only that one feature of the subject state liquidation statutes – the priority scheme for distribution of the insolvent's assets – falls outside of McCarran-Ferguson). *Idaho ex rel. Soward v. United States*, 858 F.2d 445 (9th Cir. 1988), *cert. denied*, 490 U.S. 1065 (1989); *Gordon v. United States Dept. of Treasury*, 846 F.2d 272 (4th Cir.) (*per curiam*), *cert. denied*, 488 U.S. 954 (1988). Only by overstating the respective holdings of these cases, do the petitioners discover the "direct conflict" they would have this Court resolve.

What the Court Said

Far from authoring a sweeping expansion of McCarran-Ferguson to insulate the entire state liquidation scheme from federal preemption, much less "entirely exempt[ing] anything insurance companies do" (Petition at 24), the Court of Appeals mistakenly *diminished* the statute's role in the case. Concerning preemption, the court wrote:

> If the Convention requires arbitration, it preempts provisions of the McCarran-Ferguson Act, the Federal Arbitration Act, and the State Insurance Law empowering the Superintendent to litigate on behalf of an insolvent insurance company. The focus, therefore, must be on the Convention, not the federal statutes.

(PA:8) (citations omitted). This passage suggests that McCarran-Ferguson did not influence the analysis below.[8]

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[8] The proposition that a treaty "preempts" federal statutes tends to show that McCarran-Ferguson received only passing consideration. There is no prescribed pecking order, constitutional or otherwise, that elevates treaties over statutes. A treaty is "to be regarded in the courts of justice as equivalent to an act of the legislature." *Foster v. Neilson*, 27 U.S (2 Pet.) 253, 314 (1829) (Chief Justice Marshall). "By the Constitution, laws made in pursuance thereof and treaties made under the authority of the United States are both declared to be the supreme law of the land, and no paramount authority is given to one over the other. . . ." *Chae Chan Pong v. United States*, 130 U.S. 581, 600 (1889).

However, the Court of Appeals' error in this regard only aided the petitioners because it erased McCarran-Ferguson as a limitation on the Convention and its implementing legislation. Given its proper weighting, McCarran-Ferguson insulates from preemption New York's regulatory scheme, insofar as it bars the Liquidator from arbitrating a claim for reinsurance proceeds.

The court's second reference to McCarran-Ferguson, a bare citation, is the only hook for petitioners' claim that the court "necessarily held" that the liquidation of insolvent insurers is state regulation of the business of insurance. In construing the Convention, and after acknowledging *Mitsubishi*'s admonition that the Convention's exceptions be "implemented by examining the domestic law of an acceding nation" (PA:13), the court went on to say:

> In the United States statutes provide that insurance is generally a matter of State concern and that the laws of the individual states govern (McCarran-Ferguson, 15 U.S.C. §§ 1011-1012[b], *supra*; *see also*, The Bankruptcy Act, 11 U.S.C. § 109[b][2](which exempts insurance companies from its provisions). Thus, in this case, the law to be applied in interpreting the exceptions is Article 74 of the New York Insurance Law.

(PA:14). The citation to McCarran-Ferguson suggests it was a steppingstone by which the court reached state law to interpret the Convention's exceptions – although subsequent expressions of the court's holding omit any reference to the statute.[9] In any event, the opinion features no discussion of the "business of insurance."

The "Business of Insurance"

Apart from lacking a firm foundation in the opinion below, the Petition misconceives the McCarran-Ferguson statute when it proposes the question whether "the liquidation of an insolvent insurance company falls within McCarran-Ferguson's exemption from federal law" (Petition at i). One might just as usefully ask whether the operation of a solvent insurance company falls within the McCarran-Ferguson exemption. In each

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[9] *E.g.*, "We conclude, therefore, that although the referenced agreements fall within the broad terms of the Convention, plaintiff is excepted from arbitration because the arbitration clause and the dispute alleged to be subject to it are not capable of performance and settlement under the law of New York" (PA:20-21).

case, the answer depends upon the specific activity under examination, its proximity to the core of the "business of insurance," and its place within the state regulatory scheme.

Just as some activities of operating insurance companies will not constitute the business of insurance within McCarran-Ferguson,[10] some activities of defunct insurers *will* constitute the business of insurance. The petitioners' approach — broadly excluding post liquidation activities from the business of insurance — would eviscerate McCarran-Ferguson's protection of the state regulatory scheme at a time when the need for its coherent operation is most acute.

That approach cannot be reconciled with this Court's decisions elucidating the "business of insurance," nor is it a logical outgrowth of the Fourth and Ninth Circuit decisions cited by petitioners. This Court's opinion in *S.E.C. v. National Securities, Inc.*, 393 U.S. 453, 460 (1969), generally defined the business of insurance to include:

> The relationship between insurer and insured, the type of policy which could be issued, its reliability, interpretation, and enforcement — these were the core of the "business of insurance." Undoubtedly, other activities of insurance companies relate so closely to their status as reliable insurers that they too must be placed in the same class.

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[10] "Insurance companies may do many things which are subject to paramount federal regulation; only when they are engaged in the 'business of insurance' does [McCarran-Ferguson] apply." *S.E.C. v. National Securities, Inc.*, 393 U.S. 453, 459-60 (1969). *Compare Metropolitan Life Ins. Co. v. Massachusetts*, 471 U.S. 724, 744 (1985) (state laws regulating the terms of insurance *contracts*, such as law requiring provision for mental health coverage, are laws regulating the business of insurance) *with Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119, 131 (1981) (insurer's use of chiropractic "peer review committees" to audit submitted claims not business of insurance, though such committees may assist insurer in conducting its operation); *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 214 (1978) (purchase agreements between insurer and pharmacists not business of insurance, though such agreements undoubtedly provide economic advantage to insurer).

The Liquidator's collection of reinsurance proceeds is central to the reliability of Nassau policies. During this case's excursion through the federal courts, the Second Circuit Court of Appeals observed:

> Under New York law, the Superintendent's power to collect on reinsurance agreements entered into by a liquidated company is a matter of no little concern, for policy holders have no direct right of action against reinsurers; only the Superintendent, as liquidator, can recover from the reinsurer. The extent to which the Superintendent is able to collect thus affects the degree to which the insolvent insurer's estate will have assets sufficient to satisfy the claims of its creditors.

(PA:82-83) (citations omitted).[11] For that reason, the Liquidator's collection of reinsurance proceeds is systematically facilitated by New York's regulatory scheme. The Insurance Law vests him with "title to all property, contracts and rights of action of [the] insurer as of the date of entry of the order" and provides that a liquidation order shall direct the liquidator "forthwith to take possession of the property of [the] insurer." N.Y. Ins. Law § 7405. The statute also assures that reinsurance proceeds will be payable "without diminution because of the insolvency of the ceding insurer" by requiring inclusion of a clause to that effect in the reinsurance agreement as a condition to the insurer taking credit for reinsurance on its statutory statement. N.Y. Ins. Law § 1308.[12]

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[11] Although guaranty funds often step in to fund payment of claims to policyholders, they are jurisdictionally limited with respect to the types of policyholders and claims covered and with respect to the amount of coverage. Moreover, as the United States District Court noted, the guaranty fund's own reliability is, in part, a function of its ability to recoup from the liquidation estate amounts paid to policyholders (PA:118).

[12] Absent an "insolvency clause," the Liquidator could not collect the reinsured portion of a loss without having first paid it out — a step that may be foreclosed by the insolvency. *Fidelity & Deposit Co. of Md. v. Pink*, 302 U.S. 224, 228 (1937), *reh'g denied*, 302 U.S. 780 (1938). Each of the subject reinsurance agreements has such a clause (CA:74, 83, 93).

The reinsurance arrangements of a liquidating company, and the Liquidator's collection of proceeds due under those arrangements, readily satisfy the three "business of insurance" criteria identified by this Court in *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119 (1982).[13] A reinsurance arrangement spreads the primary insurer's risk on a given policy or class of policies. Reinsurance is the "ceding by one insurance company to another of all or a portion of its risks for a stipulated portion of the premium. . . ." 13A Appleman, *Insurance Law and Practice*, § 7681 (rev. ed. 1976). Reinsurance is an "integral part of the relationship between the policyholder and the insurer" because it supports the insurer's obligations to the policyholder. *Corcoran v. Universal Reinsurance Corp.*, 713 F. Supp. 77, 82-83 (S.D.N.Y. 1989) ("[w]here an insurance carrier has financed its exposure through reinsurance, its policies are worth no more than the reinsurance behind them"). For that reason, "[r]einsurance takes on added significance when the insurer becomes insolvent." *Skandia America Reinsurance Corp. v. Schenck*, 441 F. Supp. 715, 724 (S.D.N.Y. 1977). Finally, the relationship between the insurer and reinsurer is self-evidently "limited to entities within the insurance industry," not just as a matter of practice but as a regulatory imperative. N.Y. Ins. Law § 1308(a)(1) and § 107(a)(8).

State and federal courts have recognized that reinsurance is part of the business of insurance. *In re Insurance Antitrust Litigation*, 723 F. Supp. 464, 473 (N.D. Cal. 1989) ("[t]here is no authority for excluding reinsurance from the business of insurance") (applying *Pireno*); *American Mutual Reinsurance Co. v. Calvert Fire Insurance Co.*, 52 Ill. App. 3d 922, 927, 367 N.E.2d 104, 109 (Ill App. Ct. 1977), *cert. denied*, 436 U.S. 906 (1978) ("the ultimate purpose of [a reinsurance agreement] is to provide reliable insurance to policyholders") (following *National Securities*). *See also Feinstein v. Nettleship Co. of Los*

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[13] Those criteria are "first, whether the practice has the effect of transferring or spreading a policyholder's risk; second, whether the practice is an integral part of the policy relationship between the insurer and the insured; and third, whether the practice is limited to entities within the insurance industry." 458 U.S. at 129.

Angeles, 714 F.2d 928 (9th Cir.), *cert. denied*, 466 U.S. 972 (1984) (holding that McCarran-Ferguson precludes application of federal antitrust legislation to a group of California medical insurers that included reinsurers).

The two federal circuit court decisions cited by petitioners in support of a categorical exclusion of liquidating companies from McCarran-Ferguson cannot sustain that characterization. Regardless of whether they were correctly decided, they were plainly limited to a single, and markedly different, aspect of the respective insurer liquidation statutes – the prescription of a priority scheme for distribution of the defunct insurer's assets.

In *Gordon*, the Fourth Circuit adopted, in all but one respect, the district court's holding that Maryland's statutory priority scheme was not a regulation of the "business of insurance."[14] As formulated by the lower court in that case, the "sole question is whether the State of Maryland was acting to regulate the 'business of insurance' when it established the statutory scheme regarding the liquidation of insolvent insurance companies *and the priorities of claimants or policyholders for payment*." 668 F. Supp. at 486 (emphasis supplied). The court answered only that narrow question and, regardless of whether it answered correctly, it did not decide whether the liquidation of the insolvent insurer *per se* is the business of insurance.[15]

In *Soward*, the Ninth Circuit addressed the same question and was equally at pains to curtail its holding to the single feature of Idaho's liquidation scheme that was assertedly preempted:

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[14] The Fourth Circuit declined to adopt the district court's suggestion that the first element of the *Pireno* test – that the practice has the effect of transferring or spreading a policyholder's risk – stated an "indispensable" requirement. 846 F.2d at 273.

[15] "The question of whether other portions of the Maryland Insurance Code regulate the 'business of insurance' is not before the Court and is not relevant to the Court's opinion and rulings in this case." 668 F. Supp. at 486-7, n.4.

> Idaho believes that we should not look only at § 41-3342 [setting the priority of distribution] to decide the case but should examine the entire statutory scheme erected by Idaho Insurance Code. There are several problems with this suggestion, the most obvious of which is that it begs the question. When considered as a whole, obviously the statute does seek to regulate the business of insurance; *but the question is whether the specific provision constitutes the type of regulation that Congress sought to protect from indirect federal preemption by passing the McCarran-Ferguson Act.*

858 F.2d at 454-55 (emphasis supplied). *Soward*'s holding is an answer to that specific question, not a categorical debarment of state liquidation schemes from McCarran-Ferguson's protected realm.

For the foregoing reasons, petitioners have failed to show that the Court of Appeals' decision in this case presents any actual conflict with the decisions of the Fourth and Ninth Circuits in *Gordon* and *Soward*, respectively.[16]

IV.

COMPELLING ARBITRATION WITH FOREIGN REINSURERS WOULD JEOPARDIZE THE ORDERLY LIQUIDATION OF INSOLVENT INSURERS

Enforcing arbitration clauses against the Liquidator of an insolvent insurer would seriously undermine the statutory scheme. In this regard, the industry customs and the statistics featured in the petition prove too much. To say that there has been a proliferation of insurer insolvencies within the United

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[16] Petitioners' additional argument that McCarran-Ferguson applies only to interstate commerce and not to foreign commerce (Petition at 36-39) is supported by no case authority whatsoever and is soundly defeated by the plain language of the statute, which provides that "No Act of Congress" shall preempt state regulation to the business of insurance "unless such Act specifically relates to the business of insurance..." There is no interstate commerce limitation.

States (Petition at 54-56); that a considerable proportion of the reinsurance protecting domestic insurers has been placed with foreign reinsurers (*id.* at 56-57); and that reinsurance contracts almost invariably provide for arbitration of disputes between the ceding company and the reinsurer (*id.* at 59) only demonstrates that reversal would widely affect, and materially impair, state insurer liquidation procedures.

Compelling the Liquidator to arbitrate would eradicate important substantive and procedural protections. Without ever having agreed to relinquish them, the Liquidator (and the policyholder and public interests he represents) would forfeit a judicial forum, any right of substantive appeal, and would even have to forego the scrupulous application of the pertinent law to the dispute.[17] Moreover, the New York Insurance Law, § 1213(c) provides that, before filing an answer, an unauthorized alien insurer (such as Ardra) must post security with the clerk of court in an amount sufficient to secure any judgment which may be rendered against it.[18] Section 1213(c) protects claimants against unauthorized alien insurers from litigating all the way to judgment only to find that they must go to a foreign country to obtain enforcement.[19] In arbitration under the Convention, the Liquidator would be constrained to proceed without pre-answer security. *Cf. Cooper v. Ateliers de la Motobecane*, 57 N.Y.2d 408, 456 N.Y.S.2d 728 (1982) (provisional remedy of prejudgment attachment unavailable in case falling under the Convention).

Moreover, to compel the Liquidator to arbitrate each and every reinsurance dispute and, indeed, often to compel him to arbitrate in foreign countries,[20] would grotesquely multiply the expense

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[17] The arbitration clauses provide that the arbitrators are "relieved of all judicial formalities and may abstain from following the strict rule of law" (CA:74, 82, 92).

[18] The only alternative permitted by the statute is for the alien insurer to obtain a license to conduct an insurance business in New York. N.Y. Ins. Law § 1213(c)(1)(B).

[19] This important statutory protection is not unique to New York; it is New York's enactment of the Uniform Unauthorized Insurers Service of Process Act.

[20] One of the subject reinsurance contracts provides for arbitration in Hamilton, Bermuda (CA:92).

and delay associated with marshalling the reinsurance proceeds due to the insolvency estate. Not only would the Liquidator be forced to engage counsel and maintain suit in foreign countries, he would also be constrained to pay his share of the arbitrators' fees. All of this would tax the resources of an entity that is already insolvent.

Nothing about this case requires that it become the vehicle to achieve such a result. Although petitioners make much of it, the "international" character of the arbitral agreements between the DiLoreto companies may prove to be as illusory as the agreements themselves. The Liquidator alleges that Ardra, ostensibly a Bermuda corporation, is merely an *alter ego* of the DiLoretos, who are New York residents (CA:229-236). Due to the interlocutory posture of the case, the *alter ego* claim has not yet been determined; but, after noting the companies' common ownership, the Court of Appeals did observe that "Nassau and the DiLoretos were New York residents and were amenable to process in New York," that the contracts "specifically referred to New York law in various clauses," and that the case "does not present an international merchant subjected to unfamiliar judicial proceedings and the vagaries of foreign law" (PA:19-20). If Ardra is ultimately held to be just an *alter ego* of the DiLoretos, then the case will shed any pretense of being an international controversy within the Convention's purview.

CONCLUSION

For the foregoing reasons, the petition should be denied.

Respectfully submitted,

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May 10, 1991

APPENDIX

At a Special Term, Part I of the Supreme Court of the State of New York, held in and for the County of New York, at the Court house, 60 Centre Street in the Borough of Manhattan, City and State of New York, on the 22nd day of June, 1984.

PRESENT:

HON. LEONARD N. COHEN

JUSTICE.

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Index No. 42173/1984

In the Matter of

ORDER OF LIQUIDATION

the Application of

JAMES P. CORCORAN, as Superindentent of Insurance of the State of New York, for an order to take possession of and liquidate the business of and dissolve

NASSAU INSURANCE COMPANY

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Petitioner, JAMES P. CORCORAN, Superintendent of Insurance of the State of New York, having moved this Court for an order to take possession of the property and to liquidate the business and affairs and to dissolve the corporate existence of NASSAU INSURANCE COMPANY, and such motion having duly come on before this Court on the 22nd day of June, 1984.

NOW, upon reading and filing the order to show cause made on the 18th day of June, 1984 by the Hon. Justice THOMAS J. HUGHES, one of the Justices of the Supreme Court of the State of New York, and the petition of JAMES P. CORCORAN, Superintendent of Insurance of the State of New York, verified

the 15th day of June, 1984, and the exhibits annexed thereto, with proof of due service thereof, in support of said motion, and it appearing to my satisfaction that NASSAU INSURANCE COMPANY was incorporated under the laws of the State of New York on December 2, 1964 and licensed as a stock casualty insurer in the State of New York on May 5, 1965; that its principal office is located in the County of Nassau, City and State of New York; that it is amenable to the Insurance Law of the State of New York and particularly to Article XVI thereof, and upon reading the order of rehabilitation entered in the New York County Clerk's office on the 13th day of March, 1984; Exhibit "A" annexed to the petition herein, and it appearing to my satisfaction that further efforts to rehabilitate NASSAU INSURANCE COMPANY would be futile and that the rehabilitation proceeding of the said corporation should be terminated; that it is impossible to reinsure in whole or in part the existing policy obligations of NASSAU INSURANCE COMPANY pursuant to the provisions of Section 514 (2a), Insurance Law, and that the Liquidator should be relieved of the requirement of said Section; that NASSAU INSURANCE COMPANY is insolvent; that it is in such condition that its further transaction of business would be hazardous to its policyholders, creditors or to the public; that it is to the best interests of all persons concerned that this application should be granted and NASSAU INSURANCE COMPANY should be liquidated under and pursuant to Article XVI of the Insurance Law; that it should be dissolved and its corporate charter annulled and forfeited; and petitioner having appeared by Hon. ROBERT ABRAMS, Attorney General of the State of New York, in support of said motion, and there being no appearance in opposition thereto, and after due deliberation having been had thereon and upon filing the opinion of the Court;

NOW, on motion of Hon. ROBERT ABRAMS, Attorney General of the State of New York, it is

ORDERED, that the petition of JAMES P. CORCORAN, Superintendent of Insurance of the State of New York, be and the same hereby is in all respects granted; and it is further

ORDERED, that NASSAU INSURANCE COMPANY be and it hereby is adjudged to be insolvent; and it is further

ORDERED, that the rehabilitation proceeding of the NASSAU INSURANCE COMPANY is hereby simultaneously terminated with the entry of the order herein; and it is further

ORDERED, that JAMES P. CORCORAN, Superintendent of Insurance of the State of New York, and his successors in office as Superintendents of Insurance of the State of New York, be and he is and they are hereby appointed Liquidator of NASSAU INSURANCE COMPANY, and are hereby authorized and directed forthwith to take possession of the property and liquidate the business of NASSAU INSURANCE COMPANY under and pursuant to the provisions of Article XVI of the Insurance Law of the State of New York and to deal with the property and business of NASSAU INSURANCE COMPANY in his or their names as Superintendents of Insurance and he is and they are vested with title to all of the property, contracts and rights of action of NASSAU INSURANCE COMPANY, pursuant to Section 514 of the New York Insurance Law; and it is further

ORDERED, that the notice of the aforesaid be given by publication in the editions of the New York Times and The Journal of Commerce, commencing on or about 11th day of July, 1984, and thereafter once a week for two successive weeks; and it is further

ORDERED, that the notice hereinbefore prescribed is sufficient notice to all persons interested in the assets of NASSAU INSURANCE COMPANY; and it is further

ORDERED, that formal notice of the making and entry of this order be given by the Superintendent of Insurance, as Liquidator, by mail to all policyholders, creditors and all other persons having any unsatisfied claim or demand of any character against the corporation as disclosed by the books and records of the corporation in the possession of the Superintendent of Insurance, as Liquidator, at the last known address of such persons as disclosed by said records and in such other manner and

form as he in his discretion may find desirable, demanding that all persons indebted to NASSAU INSURANCE COMPANY render accounts of their indebtedness and pay any sums due to the Superintendent of Insurance, as Liquidator; and giving notice to present proofs of claim with the Superintendent of Insurance, as Liquidator, at a place specified in such notice within twelve months from the date of the entry of this order and no later than the 30th day of June, 1985; and that such notice may contain such other rules, regulations and information as the Superintendent of Insurance, as Liquidator, may deem necessary for the purpose of this proceeding in fixing and determining all lawful and valid claims and demands against the corporation; and it is further

ORDERED, that in the event one or more Insurance Departments and/or Guaranty Funds or Associations of foreign states that have adopted the Uniform Insurers Liquidation Act in which respondent was licensed to do business, desire to give formal notice to policyholders and creditors in their respective states to present proofs of claim to the respective State Insurance Department or Guaranty Fund or Association, the Superintendent of Insurance, as Liquidator, may permit the giving of such notice as he in his discretion may find desirable; and it is further

ORDERED, that all outstanding policy and other insurance obligations of NASSAU INSURANCE COMPANY terminate and all liability thereunder cease and be fixed as of 12:01 A.M., Eastern Daylight Savings Time, on the 10th day of August, 1984, or prior thereto upon the procurement by policyholders, respectively, of new insurance covering their risks insured thereby, and notice thereof shall be given as hereinabove set forth; and it is further

ORDERED, that all other subsisting contracts, tax sharing agreements and other obligations of NASSAU INSURANCE COMPANY terminate, and all liability thereunder cease and be fixed as of the date of the entry of this order; and it is further

ORDERED, that the Superintendent of Insurance, as Liquidator, be and he hereby is relieved of the provisions set forth

in Section 514 (2a), Insurance Law, to wit: to reinsure in whole or in part the policy obligations of NASSAU INSURANCE COMPANY; and it is further

ORDERED, that JAMES P. CORCORAN, Superintendent of Insurance of the State of New York, and his successors in office as Superintendents of Insurance of the State of New York, be and he is and they are hereby authorized, permitted and allowed to sell, assign and transfer any and all of the stocks, bonds and securities in his possession or which may hereafter come into his possession belonging to NASSAU INSURANCE COMPANY, in liquidation, at market price or better, or when there is no market price, at the best price obtainable, at private sale and at such times and upon such terms and conditions as in his discretion he deems for the best interests of the creditors of NASSAU INSURANCE COMPANY, in liquidation, and that he be authorized, permitted and allowed to take such steps and to make and execute such agreements and other papers as may be necessary to effect and carry out such sales, transfers and assignments; and it is further

ORDERED, that said NASSAU INSURANCE COMPANY, its officers, directors, trustees, policyholders, agents and employees and all other persons having any property or records belonging to the said NASSAU INSURANCE COMPANY, are hereby directed to assign, transfer and deliver to the Superintendent of Insurance, as Liquidator, all of such property in whomsoever name the same may be, and that any persons, firms or corporations having any books, papers or records relating to the business of said corporation shall preserve the same and submit them to the Superintendent of Insurance, as Liquidator, for examination at all reasonable times; and it is further

ORDERED, that the officers, directors, trustees, policyolders, agents and employees of said NASSAU INSURANCE COMPANY, and all other persons be and they hereby are enjoined and restrained from the further transaction of business or from dealing with or disposing of the property or assets of said corporation, or doing or permitting to be done any act or thing which might waste its property or assets or allow or suffer the

obtaining of preferences, judgments, attachments or other liens, or the making of any levy against said corporations, or its estate while in the possession and control of the Superintendent of Insurance, as Liquidator; and it is further

ORDERED, that the officers, directors, trustees, policyholders, agents and employees of said NASSAU INSURANCE COMPANY, and all other persons, including but not limited to claimants, plaintiffs and petitioners who have claims against the said NASSAU INSURANCE COMPANY, be and they hereby are permanently enjoined and restrained from bringing or further prosecuting any action at law, suit in equity, special or other proceeding against the said corporation or its estate, or the Superintendent of Insurance of the State of New York and his successors in office as Liquidator thereof, or from making or executing any levy upon the property or estate of said corporation, or from in any way interfering with the Superintendent of Insurance of the State of New York, or his successors in office, in his or their possession, control or management of the property of said corporation, or in the discharge of his or their duties as Liquidator thereof, or in the liquidation of the business of said corporation; and it is further

ORDERED, that all parties to law suits in this state and all other states and territories of the United States, are hereby enjoined and restrained from proceeding with any pre-trial conference, trial, application for judgment, or proceeding on judgments or settlements in such actions at law, suits in equity, special or other proceedings in which NASSAU INSURANCE COMPANY is obligated to defend a party insured or any other person it is legally obligated to defend by virtue of its insurance contract for a period of 180 days from the date hereof; and it is further

ORDERED, that those persons who may have first party or New York Comprehensive Automobile Insurance Reparations Act (No Fault) policyholder loss claims against NASSAU INSURANCE COMPANY coming within the purview of Sections 330, 333 and 334 of the New York Insurance Law, are enjoined for 90 days from the date hereof from presenting and filing such

formal claims in this proceeding, pursuant to Section 543 of the New York Insurance Law; and it is further

ORDERED, that the corporate charter of said NASSAU INSURANCE COMPANY be and the same hereby is forfeited, surrendered and annulled and the said NASSAU INSURANCE COMPANY is hereby dissolved; and it is further

ORDERED, that all further papers in this proceeding shall bear the caption and be entitled;

"SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

In the Matter of

the Liquidation of

NASSAU INSURANCE COMPANY"

in place and stead of the caption as heretofore used; and it is further

ORDERED, that Superintendent of Insurance, as Liquidator, may at any time make further applications at the foot of this order for such further and different relief as he sees fit.

E N T E R

/s/ Leonard N. Cohen

J.S.C.

Supreme Court, U.S.
FILED
MAY 22 1991
OFFICE OF THE CLERK

No. 90-1567

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

ARDRA INSURANCE COMPANY, LTD., et al.,
Petitioners,

vs.

SALVATORE R. CURIALE, SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK, AS LIQUIDATOR OF NASSAU INSURANCE COMPANY, IN LIQUIDATION,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE NEW YORK STATE COURT OF APPEALS

REPLY TO BRIEF IN OPPOSITION

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May 21, 1991

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IN THE
SUPREME COURT OF THE UNITED STATES
October Term, 1990

ARDRA INSURANCE COMPANY, LTD., et al.,

Petitioners,

v.

SALVATORE R. CURIALE, SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK, AS LIQUIDATOR OF NASSAU INSURANCE COMPANY, IN LIQUIDATION,

Respondent.

Reply to Brief in Opposition

Instead of addressing the reasons for granting certiorari, the Respondent's Brief in Opposition ("Opp. Br.") raises the frivolous claim that this Court lacks jurisdiction to hear the petitioner's appeal, argues the merits of the case, attacks the lower court's order as "mistaken" in certain respects, and urges this Court to allow the decision below to stand in order not to "eradicate important substantive and procedural protections" that the Liquidator believes

he now enjoys.[1] The Liquidator's brief does not, however, undercut any of the four separate reasons for granting certiorari.[2]

A. The Liquidator argues that this Court lacks jurisdiction "[b]ecause the decision below rests on independent and adequate state law grounds." Opp. Br. at 4 (citing, *inter alia*, *Michigan v. Long*, 463 U.S. 1032 (1983)). In *Long*, however, this Court made clear that it "will not assume that a state-court decision rests on adequate and independent state grounds when the 'state court decision fairly appears to rest primarily on federal law, or to be interwoven with the federal law, and when the adequacy and independence of any possible state law ground is not

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[1] Opp. Br. at 4-6, 6-9, 10, 17.

[2] Petition for Writ of Certiorari ("Cert. Pet.") at 13-15.

clear from the face of the opinion.'" *Caldwell v. Mississippi*, 472 U.S. 320, 327 (1985) (quoting *Long*, 463 U.S. at 1040-41). *Accord New York v. P.J. Video, Inc.*, 475 U.S. 868, 872 n.4 (1986); *Michigan v. Chesternut*, 486 U.S. 567, 571 n.3 (1988).

The Liquidator himself says the lower court's citation of the McCarran-Ferguson Act "suggests [the Act] was a steppingstone by which the court reached state law to interpret the Convention's exceptions." Opp. Br. at 11. In a word, the New York State Court of Appeals applied a federal law in order to reach state law which it used to modify a federal treaty. There is no independent and adequate state law ground anywhere in that remarkable progression.[3]

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[3] The Liquidator also argues that "[s]tate law determines whether a contract containing an agreement to arbitrate is binding upon a (continued...)

B. In *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, this Court refused to "subvert the spirit of the United States' accession to the Convention by recognizing subject-matter exceptions where Congress [had] not expressly directed the courts to do so." 473 U.S. 614, 639 n.21 (1985). In contrast, the New York Court of Appeals held that the "subject matter of the claims against Ardra must be litigated in [New York] Supreme Court," relying upon its own thirty-year-old case that created a unique, judicially-implied exception to arbitrability. A:16. The court found that the arbitration clauses are "null

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[3](...continued)
particular party," Opp. Br. at 5, and cites for this proposition *Volt Information Sciences, Inc. v. Board of Trustees*, 489 U.S. 468 (1989). In *Volt*, this Court held that, where the parties had agreed in the contract to abide by state rules of arbitration, those state rules should be applied. 489 U.S. at 477. There is no such provision in the reinsurance contracts at issue here.

and void, inoperative or incapable of being performed," pursuant to Article II(3) of the Convention, and that this contract action is not a subject matter capable of settlement by arbitration, pursuant to Article II(1). Both findings are contrary to *Mitsubishi*.

The direct conflict between New York's highest court and this Court on the interpretation of a treaty merits granting the petition. *Duren v. Missouri*, 439 U.S. 357, 363 (1979). *See also Hudson v. Louisiana*, 450 U.S. 40, 42 (1981); *William E. Arnold Co. v. Carpenters Dist. Council*, 417 U.S. 12, 14 (1974); Supreme Court Rule 10.1(c). As the Court recently stated, "[t]he object of our granting writs of certiorari on points of statutory or treaty interpretation is to determine the correctness of fundamental points that lower courts have resolved . . . ." *Chan v. Korean Air*

Lines, Ltd., 490 U.S. 122, 134 n.5 (1989). The order of the court below certainly involves a fundamental issue: whether state courts can carve out exceptions to a treaty of the United States with eighty-five other nations.

The Liquidator argues that the holding below is a "straightforward" application of certain unspecified Article II(3) exceptions. Opp. Br. at 7. The Liquidator, however, cannot cite any decision from any other United States court that has made any exception to the enforcement of arbitral agreements under the Convention. He, therefore, analogizes the liquidation of an insolvent insurer to a bankruptcy proceeding and relies upon a Third Circuit decision for the proposition that "[e]nforcement of a bankrupt's arbitral agreement will be denied where arbitration 'would seriously jeopardize the objectives of the

[Bankruptcy] Code.'" Opp. Br. at 8 (quoting *Hays & Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 885 F.2d 1149, 1161 (3d Cir. 1989)).

In *Hays*, the Third Circuit held precisely to the contrary:

> Where . . . a trustee seeks to enforce a claim inherited from the debtor in an adversary proceeding in a district court, we perceive no adverse effect on the underlying purposes of the Code from enforcing arbitration -- certainly no adverse effect of sufficient magnitude to relieve a district court of its mandatory duty under the Arbitration Act as interpreted in the recent case law.

Id. The Third Circuit, relying on the "strong federal policy favoring arbitration," as set forth in this Court's recent decisions, and citing numerous other district and bankruptcy court decisions honoring arbitration agreements in pre-petition contracts, explicitly rejected the Liquidator's arguments. *Id.* at 1153 n.4, 1161 n.21.

C. The Liquidator suggests that the court below did not necessarily hold that the liquidation of an insolvent insurance company constitutes the regulation of the business of insurance under the McCarran-Ferguson Act, Opp. Br. at 9-10, faults the Court of Appeals for not discussing the reasons for its holding, Opp. Br. at 11, and even argues that the court below "mistakenly *diminished*" the McCarran-Ferguson Act's "role in the case." Opp. Br. at 10. As already noted, however, the Liquidator ultimately concedes that the statute "was a steppingstone by which the Court reached state law to interpret the Convention's exceptions." Opp. Br. at 11.

The Liquidator then attacks the reasoning of the Fourth and Ninth Circuits in *Gordon v. Department of the Treasury*, 668 F. Supp. 483 (D. Md. 1987),

aff'd, 846 F.2d 272 (4th Cir. 1988), *cert. denied*, 488 U.S. 954 (1988), and *Idaho ex rel. Soward v. United States*, 858 F.2d 445 (9th Cir. 1988), *cert. denied*, 490 U.S. 1065 (1989). These arguments do not dispel the conflict between those Circuits and the highest court of the State of New York.

The Liquidator argues, in the alternative, that even if *Soward* and *Gordon* were correctly decided, they were limited to a "single . . . aspect" of insurer insolvency, the priority of claims payments. Opp. Br. at 15. *Soward* and *Gordon* were concerned with far more than that. The District Court in *Gordon*, whose opinion the Fourth Circuit adopted, considered other aspects of the Maryland Insurance Code that dealt with insolvency and reviewed the "priority scheme" at issue in the context of the entire "statutory scheme regarding the

liquidation of insolvent insurance companies." 668 F. Supp. at 486.

The court discussed, for example, the Maryland guaranty association which pays all valid covered claims by assessing viable insurance companies, *id.* at 490, and held that "*neither the liquidation statute* nor the priority statute are an 'integral part' of the relationship between the insured and the insurer." *Id.* at 491 (emphasis added). The court considered whether the Maryland liquidation statutes provide for a form of risk transfer and concluded that they do not. *Id.* at 490. The court in *Soward* also discussed the fact that the insurer had ceased to exist and could not conceivably be subject to insurance "regulation" under any existing Idaho statute because it was no longer in existence, much less in business. 858 F.2d at 453.

In short, the New York Court of Appeals necessarily determined that the liquidation of an insolvent insurer is state regulation of the "business of insurance" under the McCarran-Ferguson Act. The Fourth and Ninth Circuits have held it is not. This conflict between the New York court and two federal Courts of Appeals merits review. *See Mackey v. Lanier Collections Agency & Serv., Inc.*, 486 U.S. 825, 828, 832 n.6 (1988); Supreme Court Rule 10.1(b).

D. The respondent seeks to defeat the Petition with irrelevant allegations. The respondent, for example, characterizes Nassau and Ardra as "the two DiLoreto companies." Opp. Br. at 3, 18. This is an attempt to inject color into the case, but has absolutely no bearing on the Petition. It is true that the Liquidator has *alleged* that Ardra is an "alter ego" of the natural defendants,

but, as he concedes, this "alter ego claim has not yet been determined." Opp. Br. at 18. Moreover, this claim is irrelevant here since it is the Liquidator, who is most certainly not an alter ego of the DeLoretos, who now stands in the shoes of Nassau, and it is the Liquidator who opposes Ardra in this case. The ownership of Ardra has nothing whatever to do with the issue of arbitrability.

The Liquidator cannot boot-strap himself out of an obligation to arbitrate this contract action, which he commenced, by relying upon allegations that are unproven and irrelevant.

E. The respondent and petitioners apparently agree on one point: the issues raised by this case are important. Opp. Br. at 16-18; Cert. Pet. at 54-60. The respondent, however, concludes with the argument that a reversal of the Court of

Appeals' order would "eradicate important substantive and procedural protections" that he, as Liquidator, now enjoys. Opp. Br. at 17.[4] The Liquidator complains that he would lose a "judicial forum," his right of appeal, a "scrupulous application of the pertinent law," and might even have to pay an "arbitrator's fee." Opp. Br. at 16-18. These objections were considered and rejected in *Mitsubishi*, 473 U.S. at 628-40. They are nothing more than a manifestation of hostility to arbitration, demonstrating the "suspicion of arbitration as a method of weakening the protections afforded in the substantive law" that this Court has directed national courts to put aside. *Rodriquez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 481 (1989).

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[4] The Liquidator does not explain, however, why other Superintendents have recently arbitrated disputes with Bermudian reinsurers. *See* Cert. Pet. at 41.

CONCLUSION

For the reasons stated above and in Ardra's Petition, a writ of certiorari should be granted.

Respectfully submitted,

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